Supreme Court, U.S.
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93 1710 APR 28 1994

No. 93-

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1993

PHILIP MORRIS INCORPORATED
(d/b/a PHILIP MORRIS U.S.A.),

Petitioner,

v.

CABARRUS COUNTY, NORTH CAROLINA,

Respondent.

On Petition for a Writ of Certiorari to the Supreme Court of North Carolina

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PETITION FOR A WRIT OF CERTIORARI

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103 pp

QUESTION PRESENTED

Whether the use of private "bounty hunters" by a county government to conduct property tax audits under a pure contingent fee arrangement violates the Due Process Clause of the Fourteenth Amendment.

Rule 29.1 Statement

The parent company of petitioner is Philip Morris Companies Inc., a publicly-owned corporation. Petitioner does not have any subsidiaries that are not wholly-owned.

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PETITION FOR A WRIT OF CERTIORARI

OPINIONS BELOW

The opinion of the Supreme Court of North Carolina in this case has been reported at 335 N.C. 227, 436 S.E.2d 828 (1993). The opinion is reproduced in the Appendix at pages 1a-6a. The order of the Supreme Court of North Carolina denying rehearing, 335 N.C. 566 (1994), is reproduced in the Appendix at page 40a. The opinion of the Court of Appeals of North Carolina in this case is reported at 108 N.C. App. 514, 424 S.E.2d 222 (1993). The opinion is re-

produced in the Appendix at pages 7a-15a. The findings of fact and conclusions of law of the North Carolina Property Tax Commission are reproduced in the Appendix at pages 16a-29a. The decision of the Cabarrus County Board of Equalization and Review is reproduced in the Appendix at pages 30a-32a. The notices issued by respondent's Assessor are reproduced in the Appendix at pages 33a-37a.

JURISDICTION

The judgment of the Supreme Court of North Carolina was entered on December 3, 1993. Petitioner's timely petition for rehearing was denied on January 27, 1994.[1] The jurisdiction of this Court is invoked under 28 U.S.C. § 1257(a).

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

The Due Process Clause of the United States Constitution, amend. XIV, sec. 1 provides that: "No State . . . shall deprive any person of life, liberty, or property without due process of law . . . ."

Relevant portions of Sections 105-273(6a) and (6b), 105-283, 105-296(a), (b), (g) and (h), 105-299, 105-312(b), (d) and (g), and 105-322(a) and (g) of the North Carolina General Statutes are set forth in the Appendix at pages 41a-52a. (In the case of minor variations in the wording or placement of certain of the

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[1] Petitioner was advised by the Office of the Clerk of this Court that due to the national day of mourning scheduled for April 27, 1994, petitions otherwise due by that date would be accepted as timely filed on April 28, 1994, under Rule 30.1.

pertinent statutory provisions during the years at issue, only the current provision is included.)

STATEMENT

Petitioner owns a manufacturing plant in Cabarrus County, North Carolina, which began operation in 1983. For each of the years 1983 through 1989, petitioner prepared and filed a North Carolina Business Personal Property Tax Return in accordance with applicable North Carolina statutes governing the imposition of local *ad valorem* property taxes. During each of the years in question, petitioner was the largest taxpayer in Cabarrus County.

A. The Audit

Pursuant to North Carolina General Statutes, N.C. Gen. Stat. § 105-299, respondent Cabarrus County hired Tax Management Associates, Inc. ("TMA") in 1988 to assist the County Assessor. TMA is a private corporation. Its work for respondent was to include the conduct of personal property tax audits that could result in a "discovery" with respect to a particular taxpayer's property. Under North Carolina law, to "discover" property includes determining whether certain property has not been listed (*i.e.*, reported on a taxpayer's tax return) and whether there has been a substantial undervaluation of property that has been listed. N.C. Gen. Stat. § 105-273(6b).

Under the express terms of the contract between TMA and respondent, TMA was to receive as its fee for services rendered "35% of taxes discovered including penalty." (App. 54a.) Of this amount, TMA was to be paid 25% after respondent's Assessor issued a notice of discovery to the taxpayer, 25% after

the taxpayer's local appeal right was exhausted, and 50% upon the earlier of actual payment by the taxpayer or the last day the taxpayer could pay the amount due without interest. *Id.* While the North Carolina General Statutes authorize the employment of private auditing firms to assist the Assessor, they are silent regarding the use of such contingent fee arrangements. *See* N.C. Gen. Stat. § 105-299.

Respondent's contract with TMA provided that TMA would audit "a reasonable sample" of the county's business personal property taxpayers. (App. 53a.) In fact, both petitioner and Cannon Mills, Inc., the two largest taxpayers in the county, were selected for audit as part of the "random selection process."[2] The North Carolina Property Tax Commission found as a fact that "[t]he discovery by the County conducted against the Taxpayer [petitioner here] was a direct result of the County's entry into the agreement with TMA." (App. 24a.)

TMA performed its discovery work by reviewing petitioner's accounting books and records and, *inter alia*, adding particular items of expense, overhead and "capitalized interest"[3] to the cost figures for petitioner's property as shown for accounting purposes. Certain adjustments were then made to reflect the age of the property. TMA did not visit petitioner's

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[2] Transcript of Proceedings Before Property Tax Commission, May 21, 1991, p. 82.

[3] "Capitalized interest" included by TMA was not interest on money borrowed to purchase personal property, but "imputed interest" reflected on petitioner's books under applicable accounting standards.

factory or undertake (or cause to be undertaken) an appraisal of any of petitioner's property.[4]

On December 20, 1989, based on TMA's audit of petitioner's books, the Assessor issued a notice of proposed discovery to petitioner for the years 1983 through 1989 in the amount of $1,325,000,000. (App. 36a-37a.) On February 2, 1990, TMA issued a report recommending that the notice of proposed discovery be revised to assert an understatement for the years 1984 through 1989 only, in the aggregate amount of $975,821,507. (App. 64a.) After receiving several communications from petitioner, the Assessor and TMA held various formal and informal meetings with petitioner's representatives. The Assessor issued his Final Decision on May 8, 1990, in which the understatements of personal property for the years 1984 through 1989 were claimed to aggregate $923,339,510. (App. 34a.)

B. Proceedings Below

On May 17, 1990, petitioner timely filed a formal request for review of the Assessor's Final Decision with the Cabarrus County Board of Equalization and Review (the "Board"). Petitioner's principal objections were that, contrary to North Carolina law, (1) TMA used book figures rather than appraised values in making its determinations,[5] (2) TMA improperly included "capitalized interest" in property values, and (3) TMA "double-counted" as personal property a substantial amount of building and equipment assets that had been taxed as real property. (App. 66a-71a.)

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[4] Application for Hearing Before Property Tax Commission, Jan. 2, 1991, Statement attached to par. 3 at p. 6.

[5] *See* N.C. Gen. Stat. § 105-283.

Following a hearing, the Board issued its decision on November 7, 1990. The Board, *inter alia,* upheld the Assessor's Final Decision to the extent of $548,499,052 in alleged personal property understatements for the years 1984 through 1989, and imposed a ten percent across-the-board penalty for late filing with respect to those understatements. (App. 30a-32a.)[6] Petitioner's liability as a result of the Board's decision was $3,608,723 in taxes and penalties, plus accrued interest. (App. 32a.)

Petitioner appealed to the North Carolina Property Tax Commission. In a Motion to Declare Discovery Null and Void, petitioner asserted, *inter alia,* that TMA's audit and the accompanying discovery violated the public policy of North Carolina and the Due Process Clause of the Fourteenth Amendment of the United States Constitution.[7] On May 24, 1991, the Property Tax Commission held that the discovery violated the State's public policy. (App. 26a.) (The Commission has no jurisdiction to decide constitutional issues. (App. 25a.))

Respondent appealed to the Court of Appeals of North Carolina. Petitioner cross-appealed in order to ensure that its constitutional issues were preserved. (Pl. Appt. Br. at 9.) In the Court of Appeals, petitioner again argued, *inter alia,* that the discovery violated both the State's public policy and the Due Process Clause of the Fourteenth Amendment. (Pl.

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[6] Approximately two-thirds of the Board's $375 million reduction was attributable to the elimination of "capitalized interest" from the calculations.

[7] Petitioner's Motion to Declare Discovery Null and Void and Motion for an Expedited Decision at 2.

Appt. Br. at 11, 19.) The Court of Appeals disagreed with petitioner's claim that its constitutional rights had been violated, but affirmed the Property Tax Commission on public policy grounds. (App. 14a-15a.) The Court of Appeals addressed the constitutional issues as follows:

> Philip Morris' cross-appeal argues that the contract and resulting discovery are also violative of its due process and equal protection rights under both the federal and state constitutions. *We do not agree.* Upon our review of the entire record and the appellant and appellee briefs of both parties, *we conclude that the matters raised and adjudicated in the Commission's Final Decision are not issues of constitutional concern,* but are simply issues dealing with the appraisal, listing, or assessment of property. As such, they were properly before the Property Tax Commission, and it is not necessary for us to review the constitutional questions Philip Morris raises in its cross-appeal.

(App. 14a-15a.) (Emphasis added.)

The North Carolina Supreme Court reversed the decision of the Court of Appeals on December 3, 1993, rejecting petitioner's public policy and Fourteenth Amendment arguments.[8] The Supreme Court dealt with petitioner's constitutional arguments as follows:

> The general rule . . . is that *absent "constitutional restraint,* questions as to public pol-

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[8] Petitioner raised its Fourteenth Amendment arguments in its brief filed with the Supreme Court of North Carolina, portions of which appear in the Appendix at pages 72a-74a.

> icy are for legislative determination." [citations omitted] Therefore, we must consider whether the legislature has determined the public policy with regard to the issue before us.

(App. 4a.) (Emphasis added.)

The Supreme Court devoted the remainder of its opinion to its rejection of petitioner's public policy argument. It therefore necessarily determined that there was no "constitutional restraint" affecting its conclusion that because the legislature did not specifically prohibit the use of contingent fee arrangements with outside auditing firms, it apparently authorized such arrangements. The case was remanded to the Court of Appeals for further proceedings. (App. 6a.)

On December 15, 1993, petitioner filed a Motion to Alter, Amend or Modify Opinion with the Supreme Court, urging that court to hear petitioner's constitutional claims or, in the alternative, to direct the Court of Appeals to hear its claims. Respondent opposed the Motion on the ground that both courts had already passed on petitioner's constitutional claims. The Supreme Court denied the Motion on December 22, 1993. Petitioner then filed a similar motion with the Court of Appeals, which was denied on January 7, 1994. Petitioner next filed a timely Motion for Rehearing with the Supreme Court, which was denied on January 27, 1994.

REASONS FOR GRANTING THE WRIT

The instant case presents a fundamental question of first impression arising under the Due Process

Clause of the Fourteenth Amendment—whether a private firm employed to assist a county tax assessor can have so meaningful a financial interest in the results of its activity as to offend constitutional notions of basic fairness with respect to the tax assessment process.

Respondent Cabarrus County follows a practice not previously considered by this Court—the use of so-called "bounty hunters"[9] (or "tax ferrets," as they have sometimes been described[10]) that are paid on a contingency basis to conduct property tax audits in assistance of the County Assessor. The practice exists in one form or another in several other counties in North Carolina, and in Kansas, Wyoming and Connecticut (and perhaps other states) as well.[11] The Supreme Court of Georgia recently declared the practice illegal as a matter of that state's public policy.

> The power to tax rests exclusively with the government. . . . In the exercise of that power, the government by necessity acts through its agents. However, this necessity does not require nor authorize the creation of a contractual relationship by which the agent contingently shares in a percentage of

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[9] *Union Pac. Resources Co.* v. *State*, 839 P.2d 356, 377 (Wyo. 1992). *See also General Motors Corp.* v. *State Tax Comm'n*, 200 Mich. App. 117, 121, 504 N.W.2d 10, 12 (1993), *appeal dismissed*, 509 N.W.2d 157 (Mich. 1993).

[10] *E.g.*, *State ex rel. Eubanks* v. *Board of Comm'rs*, 150 Kan. 143, 91 P.2d 2, 4 (1939); *but see Dillon Stores* v. *Lovelady*, 253 Kan. 274, 855 P.2d 487, 491 (1993).

[11] *See Dillon Stores*, *supra*; *Union Pac. Resources*, *supra*; *General Elec. Co.* v. *City of Bridgeport*, No. CV93 30 45 71 S. (Conn. Super. Ct. Dec. 16, 1993).

> the tax collected, and we hold that such an agreement offends public policy. The people's entitlement to fair and impartial tax assessments lies at the heart of our system, and, indeed, was a basic principle upon which this country was founded. Fairness and impartiality are threatened where a private organization has a financial stake in the amount of tax collected as a result of the assessment it recommends.

Sears, Roebuck & Co. v. *Parsons*, 260 Ga. 825, 401 S.E.2d 4, 5 (1991).[12]

The court below declined to follow Georgia's lead. Instead, it upheld the use by respondent of private auditing firms that are paid entirely on a contingent fee basis. Following the decision below, petitioner has no recourse but to ask this Court to strike down this egregious and offensive practice.

I. THIS COURT'S PRIOR DUE PROCESS DECISIONS

This Court's prior decisions in the Due Process area would appear to leave little doubt that the use of contingent fee "bounty hunters" to conduct tax audits violates the Fourteenth Amendment.

On several occasions, this Court has considered the question whether the financial interest of a state official acting in an adjudicatory capacity creates a bias factor so strong that it results in a violation of the complaining party's Due Process rights. In *Tumey* v. *Ohio*, 273 U.S. 510 (1927), the fountainhead case in

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[12] In addition, at least two states have prohibited the practice. *See* Utah Code Ann. § 59-2-703(2)(c) (1994); Colo. Rev. Stat. § 39-10-107(1) (1993).

this area, this Court unanimously concluded that a Due Process violation resulted under a set of Ohio statutes authorizing the mayor of a village to impose fines for liquor law infringements, where the fines collected were used in part as a salary supplement to reimburse the mayor for costs incurred in conducting the trials.

This Court extended the *Tumey* doctrine in *Ward* v. *Village of Monroeville*, 409 U.S. 57 (1972). There, a mayor was authorized to impose fines for traffic violations, with the money so collected being used to provide funds for village operations. The mayor's responsibility for maintaining village finances provided a sufficient stake in the outcome of the proceedings to taint the process. The fact that the mayor did not personally benefit from the fines collected was not sufficient to distinguish *Ward* from *Tumey*. The further fact that the convicted party had the opportunity for a trial *de novo* in the county court also was not considered sufficient to cure the constitutional defect. Rather, the failure to afford the defendant a "neutral and detached" judge at the first stage of adjudication was considered a fatal flaw in the statutory scheme. 409 U.S. at 62.[13]

In *Marshall* v. *Jerrico, Inc.*, 446 U.S. 238 (1980), this Court drew a distinction between the "adjudicatory" functions that were performed in *Tumey* and *Ward*, and the "prosecutorial" function there before it. *Jerrico* involved a regional administrator responsible for enforcing the federal child labor laws. Because the administrator's role was more akin to that

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[13] *See also Connally* v. *Georgia*, 429 U.S. 245 (1977); *Gibson* v. *Berryhill*, 411 U.S. 564 (1973).

of zealous prosecutor than dispassionate adjudicator, this Court held that there was a greater burden placed on the complaining party to show that the possibility of bias had so infected the process as to result in a Due Process violation.

This Court concluded in *Jerrico* that the factors that might have biased the administrator's enforcement activities (the penalties collected were to flow back to the enforcement agency, which had authority to allocate them among the various regional offices) were "too remote" to give rise to a Due Process violation. 446 U.S. at 251. In so holding, this Court expressly left open the question of what degree of personal or financial interest might taint a prosecutor's role:

> A scheme injecting a personal interest, financial or otherwise, into the enforcement process may bring irrelevant or impermissible factors into the prosecutorial decision and in some contexts raise serious constitutional questions. * * *
>
> In this case, we need not say with precision what limits there may be on a financial or personal interest of one who performs a prosecutorial function,[12] for here the influence alleged to impose bias is exceptionally remote. No governmental official stands to profit economically from vigorous enforcement of the child labor provisions of the Act.
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> * * *

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[12] In particular, we need not say whether different considerations might be held to apply

> if the alleged biasing influence contributed to prosecutions against particular persons, rather than to a general zealousness in the enforcement process.

446 U.S. at 249-50. (Footnote in original.)

* * *

The instant case presents the financial interest question in a context that is part *Tumey/Ward*, part *Jerrico*, and part one step removed from both lines of cases. The unusual combination exists because of uncertainty regarding the nature of the tax assessor's function.

Respondent's Assessor is charged with enforcing the State property tax laws applicable in Cabarrus County. The Board of County Commissioners is authorized by statute to employ private firms "to assist" the Assessor in carrying out his duties. N.C. Gen. Stat. § 105-299. That was done in the instant case because the County had no auditors of its own. (Appt.'s New Br. at 21.)

The Assessor is responsible for reviewing property listings to determine whether additional property should be listed and whether listed property should be revalued. After providing a notice of "discovery" to a taxpayer, the Assessor may hold meetings with the taxpayer before issuing his "final decision." N.C. Gen. Stat. § 105-312(d). He also has subpoena powers to permit the gathering of additional evidence. N.C. Gen. Stat. § 105-296(g).

Here, a proposed notice of discovery was issued on December 20, 1989, in the amount of $1,325,000,000. After receiving several communications from petitioner and a report from TMA recommending a

discovery of over $975 million, the Assessor and TMA held a series of meetings with petitioner's representatives. The Assessor then issued his Final Decision on May 8, 1990, asserting the discovery of over $923 million in understated personal property.

This Court has taken seemingly conflicting positions on the nature of the tax assessor's role. One hundred years ago, this Court observed that an official charged with determining the proper value of property for purposes of *ad valorem* taxation performed a judicial function. In *Hagar* v. *Reclamation District No. 108*, 111 U.S. 701 (1884), Justice Field declared:

> But where a tax is levied on property not specifically, but according to its value, to be ascertained by assessors appointed for that purpose upon such evidence as they may obtain, a different principle comes in. *The officers in estimating the value act judicially*; and in most of the states provision is made for correction of errors committed by them, through boards of revision or equalization, sitting at designated periods provided by law to hear complaints respecting the justice of the assessments. . . .*

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* That the duties of assessors in estimating the value of property for purposes of general taxation are judicial, see *Barhyte* v. *Shepherd*, 35 N.Y. 238, 250; *Hassan* v. *Rochester*, 67 *id.* 528, 536; *Stuart* v. *Palmer*, 74 *id.* 183; *Williams* v. *Weaver*, 75 *id.* 30, 33; Cooley, Law of Taxation, 266; Burroughs, Law of Taxation, sec. 102; *Jordan* v. *Hyatt*, 3 Barb.

> 275, 283; *Ireland* v. *Rochester*, 51 *id.* 416, 430, 431; *The State* v. *Jersey City*, 24 N.J. Law (4 Zabr.), 662, 666; *The State* v. *Morristown*, 34 N.J. Law (5 Vroom), *id.* 445; *Griffin* v. *Mixon*, 38 Miss. 424, 437, 438.

111 U.S. at 710. (Emphasis added; footnote in original.)

Yet, in *Arkansas Corporation Commission* v. *Thompson*, 313 U.S. 132 (1941), this Court through Justice Black suggested a contrary view: "[A]d valorem taxes depend upon a determination of value. The governmental function of fixing the value for tax purposes has rarely, if ever, been a judicial function." 313 U.S. at 142-43.

Resolution of this apparently conflicting view of the role of the property tax assessor is a critical threshold question presented by the instant case. To the extent the Assessor has acted in a judicial or quasi-judicial capacity in issuing his discovery, the *Tumey/Ward* line of cases has direct application. If any portion of the taxes collected as a result of the audit were paid directly to the Assessor (or to his Office, as distinguished from the County generally), a Due Process violation would surely be deemed to have occurred under *Tumey* and/or *Ward*. Can the result possibly be different merely because such a payment was instead to be made to a private firm that assisted the Assessor in making the discovery?

If the Assessor's role is viewed more as that of prosecutor, however, *Marshall* v. *Jerrico* becomes directly relevant. Paying the Assessor (as "prosecutor") a contingent fee based on his determination of tax liability would actually present a situation going far

beyond what was involved in *Jerrico*, or even in *Concrete Pipe & Products, Inc.* v. *Construction Laborers Pension Trust*, ___ U.S. ___ , 113 S. Ct. 2264 (1993), the only case thus far to have addressed the question left open in *Jerrico*. (In *Concrete Pipe*, the fiduciary obligation of the trustees of a multi-employer pension fund suggested the possibility of bias in their determination of the amount of a withdrawing employer's liability to the fund.)

Again, there surely could be no meaningful difference between a contingent fee paid directly to the Assessor acting as a "prosecutor" and a contingent fee paid to his assistant who conducted the tax audit on which the Assessor relied to make his determination of liability. A Due Process violation would necessarily exist in both circumstances or in neither. Consequently, if the Assessor is seen as more of a prosecutor than a judge, the instant case finally presents for resolution the precise issue expressly left open in *Jerrico* but not fully explored in *Concrete Pipe*.

Here, the Assessor had no auditors on his staff. He relied entirely on TMA for assistance. TMA was to be paid solely and exclusively on a contingent fee basis. It is hard to imagine a situation where the "assistant prosecutor" responsible for the case would have a greater stake in the outcome of the proceedings.[14]

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[14] If, at the conclusion of its audit work, TMA had "discovered" that no understatements had occurred, it would have been paid nothing for its efforts under the terms of its contract. TMA had to find understatements in order to be compensated for its services. Moreover, the greater the additional tax liability it

II. THE REVIEW PROCEDURE DOES NOT CURE THE DUE PROCESS VIOLATION

If the Assessor is acting in a judicial or quasi-judicial capacity in the instant case, the bias resulting from TMA's contingent fee contract has thoroughly infected the process under *Tumey* and/or *Ward*. The nature of the review procedure under North Carolina law is therefore immaterial. Even a true *de novo* review at the next stage of the proceedings could not remove the taint in such circumstances. *Ward*; *Jerrico*, 446 U.S. at 247 n.9.

If the Assessor is acting as a prosecutor, the analysis is somewhat different. The question left open in *Jerrico*—how much of a financial interest on the part of the prosecutor will cause a Due Process violation—must contemplate the possibility that if the prosecutor's interest is sufficiently strong, no type of review could cure the defect. Petitioner believes that is in fact the situation here. But if the bias engendered by the contingent fee arrangement is not considered sufficient to give rise to a "*per se*" Due Process violation, then under *Jerrico* and *Concrete Pipe* it becomes necessary to determine whether the suspect influences can be cleansed at the first stage of review.

Under North Carolina law, tax assessments are clearly not reviewed *de novo* at the first stage of the proceedings. Such assessments are presumed to be correct, and are overturned only if the taxpayer can show that (i) the method used to determine them was either "illegal" or "arbitrary," and (ii) the method

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could propose, the greater its compensation was likely to be, because there was no ceiling on the amount it could earn under the contract.

produced "substantial" misvaluations.[15] It is clear, therefore, that the review process cannot play a cleansing role here.

The restricted nature of the review accorded the "prosecutor's" determination by the County Board of Equalization and Review preserves the bias in that determination generated by the contingent fee contract. Even assuming it could be shown that the assessment method used was arbitrary or illegal, any resulting changes in valuation that are not "substantial" cannot be overturned.

The instant case thus falls on the far side of the line established in *Concrete Pipe*. There, a distinction was drawn between first stage adjudications involving a "preponderance of the evidence" standard of proof and adjudications involving standards such as "clearly erroneous" and "unreasonable." 113 S. Ct. at 2279. This Court noted that the latter terms describe a standard of review that implies a degree of deference to be given to factual determinations. *Id.* This Court pointed out that if either of the latter two standards were to be employed in the hearing on review in *Concrete Pipe*, "there would be a substantial question of procedural fairness under the Due Process Clause." *Id.* at 2281.

Here, the standard of review requires at a minimum that any misvaluations be shown to be "substantial." As a result, "insubstantial" revaluations on an item-by-item basis have the potential for producing a significant tax assessment that could be immune from adjustment on review. The Board could be asked to

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[15] *See, e.g., Appeal of Amp Incorporated*, 287 N.C. 547, 562-63; 215 S.E.2d 752, 761-62 (1975) and cases there cited.

review a discovery that could well be excessive in the aggregate and that, at the same time, would carry with it a presumption of correctness that could not be rebutted. That is not the type of review that can cleanse bias in the original determinations.[16]

Moreover, given the nature of the arrangement between respondent and TMA, it is clear that the review process before the Board could not be totally unbiased in any event. Under the contract as drafted, TMA earned its fee when the notice of discovery was issued. That would appear to place the Board under considerable pressure to preserve at least 35 percent of the proposed assessment under all circumstances, in order to ensure that enough tax would be collected from petitioner at least to have sufficient funds to pay TMA.[17] In reality, petitioner had no meaningful opportunity for full and proper relief after a fair and impartial hearing such as this Court found existed in *Jerrico*.

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[16] That petitioner failed to reduce the discovery below $548 million strongly indicates that the review process was not the type of *de novo* review contemplated by *Jerrico* and *Concrete Pipe*. *See* note 6, *supra*.

[17] Petitioner understands that there is presently pending in the North Carolina courts a lawsuit between TMA and respondent regarding the proper interpretation of the contract. (*Tax Management Associates, Inc.* v. *Cabarrus County*, Superior Court of Cabarrus County, No. 93-CvS-847.) However, that lawsuit, which seeks $1,270,500 in fees from the County, was not commenced until May 7, 1993, well after the Board's review process had been completed in the instant case.

III. STATES NEED TO BE INFORMED AS TO THE CONSTITUTIONALITY OF THE "BOUNTY HUNTER" PRACTICE

Resolution of the issue here presented is necessary at this time because of the extensive litigation developing in the state courts. Within the last three years, the "bounty hunter" practice has been challenged in the Supreme Courts of five states and the lower courts of another.[18] In Georgia, the practice was struck down as violative of that state's public policy.[19] In the other five states the practice was upheld, although in one state no contingent fee was involved.[20]

Given the increasing attention that is being devoted to these arrangements, the decision below, if left unreviewed, could cause other states to begin utilizing contingent fee "bounty hunters" without a clear indication as to the constitutionality of the practice. A definitive resolution of the Due Process question is therefore essential at this time if, as petitioner believes, this Court's prior decisions in this area strongly suggest that the practice is constitutionally impermissible.

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[18] Georgia, Wyoming, Michigan, Kansas and North Carolina, as well as Connecticut.

[19] *Sears Roebuck & Co.* v. *Parsons*, *supra*.

[20] *General Motors Corp.* v. *State Tax Comm'n*, *supra* (Michigan—no contingent fee); *Union Pac. Resources Co.* v. *State*, *supra* (Wyoming); *Dillon Stores* v. *Lovelady*, *supra* (Kansas); the decision below (North Carolina); and *General Elec.*, *supra* (Connecticut).

IV. PETITIONER WILL HAVE NO FURTHER OPPORTUNITY FOR A HEARING ON ITS DUE PROCESS CLAIM

Review of the decision below by this Court effectively constitutes petitioner's final opportunity to obtain a hearing on its constitutional claims. Petitioner has continually urged its constitutional arguments, beginning with its first appearance before the Property Tax Commission in May 1991. Both the Court of Appeals and the Supreme Court of North Carolina rejected the arguments in their respective opinions. When the case was remanded for further proceedings, petitioner moved both lower courts to have its constitutional arguments addressed. Respondent then pointed out that petitioner's arguments had already been rejected, explicitly by the Court of Appeals and implicitly by the Supreme Court. (Cabarrus Cty. Response in Opp., N.C. Sup. Ct., Dec. 20, 1993, at 2-3; Cabarrus Cty. Response in Opp., N.C. Ct. App., Dec. 30, 1993, at 5-7.) Petitioner's motions were denied. (App. 38a-39a.) It is clear that only computational issues remain to be decided below. There is absolutely no prospect that petitioner's constitutional claims will be reconsidered by the lower courts.

The instant case thus falls squarely within the broad scope of the "final judgment" rule summarized in *Cox Broadcasting Corporation* v. *Cohn*, 420 U.S. 469 (1975). Both the majority and the dissent in *Cox* agreed that a case in the posture of the instant case is fully ripe for review by this Court. *See* 420 U.S. at 480, and at 506 (Rehnquist, J., dissenting) (recognizing finality "where the federal question decided by the highest court of the State is bound to survive and be presented for decision here regardless of the outcome of future state-court proceedings").

* * *

The payment of unlimited contingent fees to those hired to conduct tax audits as part of the tax assessment process clearly offends basic notions of fundamental fairness under the Due Process Clause. Whether this Court chooses to invoke the *Tumey* rule or resolve the question left open in *Jerrico*, it should now decide whether North Carolina and those other States that rely on contingent fee contracts with outside auditors in administering their tax laws are violating the Due Process Clause.

CONCLUSION

For all of the foregoing reasons, the petition for a writ of certiorari should be granted.

Respectfully submitted,

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Counsel for Petitioner

April 28, 1994

IN THE SUPREME COURT OF NORTH CAROLINA

No. 49PA93-Property Tax Commission

In the Matter of:
The Appeal of Philip Morris U.S.A. from the decision of the Cabarrus County Board of Equalization and Review for personal property taxes years 1984-1989

FILED
DEC 3 1993
IN THE OFFICE OF
CLERK SUPREME COURT
OF NORTH CAROLINA

On discretionary review pursuant to N.C.G.S. § 7A-31 of a decision of the Court of Appeals, 108 N.C. App. 514, 424 S.E.2d 222 (1993), affirming a final decision of the North Carolina Property Tax Commission. Heard in the Supreme Court on 13 September 1993.

Parker, Poe, Adams & Bernstein, by Charles C. Meeker; and Blakeney & Alexander, by David L. Terry, for the appellant Cabarrus County.

Hunton & Williams, by William S. Patterson, Jean Gordon Carter, James W. Shea, and David A. Agosto, for the appellee Philip Morris U.S.A.

Robinson Maready Lawing & Comerford, by Michael L. Robinson, on behalf of Durham County, amicus curiae.

James B. Blackburn III, General Counsel, N.C. Association of County Commissioners, and S. Ellis Hankins, General Counsel, N.C. League of Municipalities, amici curiae.

Floyd Allen & Jacobs, by Jack W. Floyd and Robert V. Shaver, Jr., on behalf of Guilford Mills, Inc., amicus curiae.

Poyner & Spruill, by J. Phil Carlton, on behalf of Investment North Carolina, Inc., amicus curiae.

S. Davis Phillips, Secretary of Commerce, on behalf of The North Carolina Economic Development Board, amicus curiae.

Johnson Gamble Mercer Hearn & Vinegar, by Charles H. Mercer, Jr., and M. Blen Gee, Jr.; and Maupin Taylor Ellis & Adams, P.A., by Charles B. Neely, Jr., Nancy S. Rendleman, and Linda F. Nelson, on behalf of North Carolina Citizens for Business and Industry, amicus curaie.

MITCHELL, Justice.

The controlling facts in this case are undisputed. In May of 1988, the Cabarrus County Tax Assessor entered into a contract, denominated "Business Personal Property Audit Agreement," with Tax Management Associates, Inc. ("TMA"). The Cabarrus County Board of Commissioners approved the contract on 16 January 1989. Under the terms of the contract, TMA agreed to provide Cabarrus County with audit services "on a reasonable sample of the County's business personal property taxpayers" in accordance with applicable North Carolina General Statutes, specifically N.C.G.S. §§ 105-283, 105-317.1 and 105-312. The fee arrangement provided for in the contract required Cabarrus County to pay TMA thirty-five percent of taxes owed on property TMA discovered, including any penalties. To "discover" property in this context means to identify taxable property that was not listed for taxation or property that was listed but was substantially undervalued in its listing by the taxpayer. *See* N.C.G.S. § 105-272(6b) (1992).

In November of 1988, TMA contacted Philip Morris U.S.A. to initiate an audit of the tax returns of Philip Morris for the years 1986 and 1987. The audit was later expanded to include Philip Morris' tax returns for all years from 1983 through 1989 and resulted in the "discovery" of a substantial amount of taxable property. Based on the audit and acting pursuant to N.C.G.S. § 105-312, the Cabarrus County Tax Assessor issued a final decision concluding that understatements of tangible personal property on the tax returns of Philip Morris exceeded $100 million per year for each of the years 1984 through 1989 and cumulatively totaled $923,339,510. Philip Morris filed a formal request for a review of the Tax Assessor's final decision by the Cabarrus County Board of Equalization and Review. A hearing was held, and in a decision dated 7 November 1990, the Board ordered an assessment of discovered personal property in the amount of $599,426,934.

Philip Morris then appealed to the North Carolina Property Tax Commission ("Commission"). Philip Morris included among its ground for appeal a contention that the contingent fee contract for private auditing services between Cabarrus County and TMA was against public policy and rendered the discovery of Philip Morris' property void. The Commission, sitting as the State Board of Equalization and Review, heard arguments of counsel and received exhibits on the parties' motions. On 24 May 1991, the Commission rendered its final decision concluding by a 3-2 vote that the contingent fee contract "was void as against public policy from its inception." Therefore, the Commission held that Cabarrus County's discovery and assessment of Philip Morris' property was void "because it resulted directly from the County's entry into a contingent fee contract that was void as against public policy."

Cabarrus County gave notice of appeal to the Court of Appeals. Philip Morris then filed a cross-notice of appeal. The Court of Appeals affirmed the decision of the Com-

mission. On 11 March 1993, this Court allowed Cabarrus County's petition for discretionary review.

Cabarrus County contends that the Court of Appeals erred in concluding that the contingent fee contract for a private tax auditor's service in the present case violates public policy. We agree and, therefore, reverse the decision of the Court of Appeals.

Only a few courts in other jurisdictions have considered the validity of contingent fee contracts for tax audits. The results reached by those courts are completely mixed and establish no clear line of authority. *E.g., Jackson Lumber Co. v. McCrimmon*, 164 F. 759 (N.D. Fla. 1908) (contingent fee arrangement not against public policy); *Sears, Roebuck and Co. v. Parsons*, 260 Ga. 824, 410 S.E.2d 4 (1991) (contingent fee contract violates public policy); *Simpson v. Silver Bow County*, 87 Mont. 83, 285 P. 195 (1930) (contingent fee contract not against public policy); *Murphy v. Swanson*, 50 N.D. 788, 198 N.W. 116 (1924) (contingent fee contract violates public policy). We do not find such authorities from other jurisdictions persuasive or particularly helpful in resolving the issue before us in this case.

The general rule in North Carolina is that absent "constitutional restraint, questions as to public policy are for legislative determination." *State v. Whittle Communications*, 328 N.C. 456, 470, 402 S.E.2d 556, 564, *reh'g denied*, 328 N.C. 735, 404 S.E.2d 878 (1991) (quoting *Gardner v. North Carolina State Bar*, 316 N.C. 285, 293, 341 S.E.2d 517, 522 (1986)). Therefore, we must consider whether the legislature has determined the public policy with regard to the issue before us.

North Carolina General Statute § 105-299 authorizes boards of county commissioners to employ firms to assist county tax assessors. It expressly provides that the "board of county commissioners may employ appraisal firms, mapping firms or other persons or firms having expertise in one or more duties of the assessor to assist him or her

in the performance of such duties." N.C.G.S. § 105-299 (1992). The General Assembly has, therefore, specifically authorized each county to employ private auditors, and we conclude that a power incidental to that grant of authority is the power to decide the basis upon which the private auditors are to be employed. Thus, the statute is the expression of the legislature regarding the public policy on this matter.

Our legislature has specifically prohibited contingent fees in certain settings when it has deemed them to be contrary to the interests of the public. For example, North Carolina law prohibits real estate appraisers giving valuations based on contingent fee arrangements, N.C.G.S. § 93A-80(a)(3), and N.C.G.S. § 120-47.5 outlaws contingent fees for lobbying. Therefore, we conclude that had the General Assembly intended that private tax auditors employed to assist county tax assessors be restricted to an hourly wage or to fixed fee remuneration, it would have expressly said so. Additionally, North Carolina courts have long upheld contingent fee contracts when they are entered into, *inter alia*, in good faith and without undue influence. *See, e.g., High Point Casket Co. v. Wheeler*, 182 N.C. 459, 109 S.E. 378 (1921) (fee of one-third of recovery held not unreasonable); *In re Foreclosure of Cooper*, 81 N.C. App. 27, 344 S.E.2d 27 (1986) (contingent fee contract approved in equitable distribution proceeding).

It is clear that our legislature is well aware of the existence of contingent fee contracts and knows how to forbid then when it wishes to do so, but it has chosen not to place any restriction on such contracts in N.C.G.S. § 105-29. Therefore, we conclude that our legislature has determined that contingent fee contracts for private tax auditor's services are not contrary to public policy. *Cf. Mazza v. Medical Mut. Ins. Co.*, 311 N.C. 621, 627, 319 S.E.2d 217, 221 (1984) (absence of legislative prohibition held to support the validity of insurance contracts covering punitive damages). We express no opinion on the wisdom of

any public policy established by the legislature, of course, as the determination of whether a particular policy is wise or unwise is for determination by the General Assembly. *Martin v. Housing Corp.*, 277 N.C. 29, 41, 175 S.E.2d 665, 671 (1970).

For the foregoing reasons, we conclude that the Court of Appeals erred in holding that the contingent fee contract in question here was void as against public policy and in holding that the resulting discovery of taxable property of Philip Morris was null and void. The decision of the Court of Appeals is reversed and this case is remanded to that court for further proceedings not inconsistent with this opinion.

REVERSED AND REMANDED.

NORTH CAROLINA COURT OF APPEALS

NO. 9110PTC762

Property Tax Commission
90-PTC-426

In the Matter of:
The Appeal of Philip Morris U.S.A. from the decision of the Cabarrus County Board of Equalization and Review for personal property taxes years 1984-1989

FILED

5 January 1993

APPEAL by Cabarrus County from a Final Decision of the Property Tax Commission entered 24 May 1991. Appeal and cross-appeal by Philip Morris U.S.A. from the same Final Decision. Heard in the Court of Appeals 26 August 1992.

Parker, Poe, Adams & Bernstein, by Charles C. Meeker, for Cabarrus County.

Hunton & Williams, by William S. Patterson, Jean Gordon Carter, James W. Shea, and David A. Agosto, for Philip Morris U.S.A.

James B. Blackburn III and S. Ellis Hankins, on behalf of the North Carolina Association of County Commissioners and the North Carolina League of Municipalities, amici curiae.

Poyner & Spruill, by Wilson Hayman, on behalf of Investment North Carolina, Inc., amicus curiae.

Floyd Allen & Jacobs, by Jack W. Floyd and Robert V. Shaver, Jr., on behalf of Guilford Mills, Inc., amicus curiae.

Johnson Gamble Mercer Hearn & Vinegar, by Charles H. Mercer, Jr. and M. Blen Gee, Jr., and Maupin Taylor Ellis & Adams, P.A., by Charles B. Neely, Jr. and Nancy S. Rendleman, on behalf of North Carolina Citizens for Business and Industry, amicus curiae.

Charles Ewart, Thomas W. Ramseur, Thomas W. Dayvault, and Carroll D. Gray, on behalf of the North Carolina Association of Chamber of Commerce Executive, the Concord-Cabarrus County Chamber of Commerce, the Kannapolis Chamber of Commerce, and the Charlotte Chamber of Commerce, amici curiae.

LEWIS, Judge.

The question posed to us by this appeal appears to be one of first impression in North Carolina. We are asked to determine whether a contingent fee contract between a county tax assessor and a private auditing firm is void as against public policy. We hold that, under the facts of this particular contract, it is, and affirm the Final Decision of the North Carolina Property Tax Commission.

In May 1988, the tax assessor of Cabarrus County entered into a Business Personal Property Audit Agreement ["agreement"] with Tax Management, Associates, Inc. ("TMA"). The Cabarrus County Board of Commissioners accepted the contract on 16 January 1989. TMA agreed to provide Cabarrus County with audit services "on a reasonable sample of the County's business personal property taxpayers," in accordance with applicable North Carolina General Statutes, specifically §§ 105-283, 105-317.1, and 105-312. The fee arrangement set between the parties required Cabarrus County to pay to TMA thirty-five percent of taxes discovered, including penalty. Philip Morris U.S.A.

("Philip Morris") contends such a contract is (1) void as against public policy and (2) unconstitutional.

Philip Morris has a cigarette manufacturing facility in Cabarrus County which has the capacity to produce 83 billion cigarettes a year. The company is the largest taxpayer in Cabarrus County. In November 1988, TMA contacted Philip Morris to initiate an audit of its records.

In December 1989, following an audit of Philip Morris for the years 1983-1989, the Cabarrus County tax assessor proposed discovery for those years in the amount of $1,325,000,000.00 plus penalties. To discover property means to determine property that was not listed or property that was listed but was substantially undervalued in its listing by the taxpayer. *See* N.C.G.S. § 105-273(6b) (1992). On 8 May 1990, the assessor issued his final decision regarding discovery of Philip Morris' personal property. The discovery from this decision included the years 1984-1989, and totaled $923,339,510.00.

Pursuant to N.C.G.S. § 105-312(d) (1992), Philip Morris requested review by the Cabarrus County Board of Equalization and Review. After a hearing, the Board reduced the amount of the discovery to $599,426,934.00. Philip Morris, on 2 January 1991, filed an Application for Hearing before the Property Tax Commission ("Commission"), seeking review of the Board's decision. On 10 May 1991 Philip Morris filed a "Motion to Declare Discovery Null and Void." In both the appeal and the motion, Philip Morris contended that TMA had no legal standing or authority to conduct and audit because the agreement between Cabarrus County and TMA was "void, illegal, illusory and against public policy."

The Final Decision of the Property Tax Commission was entered 24 May 1991. In this 3-2 decision, the Commission concluded that the appeal was properly before it, and that it had the duty to rule upon all issues concerning listing, appraisal, and assessment of property, but not those of

constitutional law. N.C.G.S. § 105-290(b) (1992). The Commission then found that the contract between TMA and Cabarrus County was "void as against public policy from its inception," and therefore adjudged the discovery null and void.

The Commission reasoned that the contingent fee arrangement as set out in the agreement "so offended conventional standards requiring fair, impartial, and uniform treatment of this State's taxpayers that [the contract] could not stand." The Commission concluded:

> The fundamental rule of our system of property taxation is that the tax will be administered in a fair, impartial, and uniform manner, without regard to the identity of the property owner. This principle cannot be followed where a county enters into a contract such as the one presented here.

Cabarrus County appealed. In an effort to preserve its right to appellate review of the issues raised in the decision, Philip Morris filed a cross-notice of appeal to this Court.

The scope of our review of the Property Tax Commission's Final Decision is governed by N.C.G.S. § 105-345.2 (1992). *In re McElwee*, 304 N.C. 68, 73-74, 283 S.E.2d 115, 119 (1981), *appeal after remand*, 75 N.C. App. 658, 331 S.E.2d 265 (1985). The *McElwee* Court held that the provisions found in N.C.G.S. § 105-345.2 and N.C.G.S. § 150A-43 (now 150B) are

> remarkably identical. . . . Subsection (a) provides that the appellate court shall review the record and exception and assignments of error in accordance with the Rules of Appellate Procedure. Subsection (b) provides that the appellate court shall (1) decide all relevant questions of law, (2) interpret constitutional and statutory provisions,

> and (3) determine the meaning and applicability of the terms of any Commission action.
>
> More importantly, with respect to this appeal, G.S. 105-345.2(b) provides that the court may (1) affirm, (2) reverse, (3) declare null and void, (4) remand for further proceedings, or (5) reverse or modify the decision of the Property Tax Commission if the substantial rights of the appellants have been prejudiced because the Commission's findings, inferences, conclusions or decisions are:
>
> (1) In violation of constitutional provisions; or
>
> (2) In excess of statutory authority or jurisdiction of the Commission; or
>
> (3) Made upon unlawful proceedings; or
>
> (4) Affected by other errors of law; or
>
> (5) Unsupported by competent, material and substantial evidence in view of the entire record as submitted; or
>
> (6) Arbitrary or capricious.
>
> G.S. 105-345.2(c) provides that the court shall review the whole record and due account shall be taken of the rule of prejudicial error.

Id.

The question is whether the contingent fee arrangement for auditing services violates public policy. Chapter 105 of the North Carolina General Statutes answers neither yea nor nay on this particular issue. Section 299 does, however, allow county boards of commissioners to employ appraisal firms "or other persons or firms having expertise in one or more of the duties of the assessor to assist him or her in the performance of such duties." N.C.G.S. § 105-299 (1992). This provision, however, does not give authority for contingent fee compensation schemes.

We note that contingent fee contracts are prohibited in at least two instances: One, for lobbying fees pursuant to N.C.G.S. § 120-47.5 (1992); and two, for real estate appraisal assignments pursuant to N.C.G.S. § 93A-80(a)(3) (Cum. Supp. 1992). We cannot agree with Cabarrus County that in the absence of a specific bar, the Legislature intended to allow contingent fee auditor contracts. Conversely, we are aware of no instances where the General Statutes permit contingent fee arrangements for State business.

We find no North Carolina case law on point addressing a contingent fee contract for auditing services. There are cases dealing with other types of contingent fee contracts. It is well-settled in North Carolina that contingent fee contracts for representation in a divorce proceeding are void, *Thompson v. Thompson*, 313 N.C. 313, 328 S.E.2d 288 (1985), as are contingent fee contracts for representation for alimony or child support. *Davis v. Taylor*, 81 N.C. App. 42, 344 S.E.2d 19, *disc. rev. denied*, 318 N.C. 414, 349 S.E.2d 593 (1986). On the other hand, contingent fee arrangements in equitable distribution actions are valid so long as they do not compensate the attorney for securing the divorce. *In re Cooper*, 81 N.C. App. 27, 344 S.E.2d 27 (1986). They are almost universally used by counsel in personal injury and wrongful death actions.

Contrary to Cabarrus County's arguments, the cases cited above do not directly guide our decision in the present case. However, one important proposition comes out of them. In a case dealing with attorney contingent fee contracts, this Court stated: "Contracts for contingent fees . . . are closely scrutinized by the courts where there is any question as to their reasonableness." *Harmon v. Pugh*, 38 N.C. App. 438, 444, 248 S.E.2d 421, 424 (1978), *disc. rev. denied*, 296 N.C. 584, 254 S.E.2d 33 (1979). We do so now.

North Carolina's tax policy is grounded in notions of fairness and equity, as mandated by the North Carolina Constitution. N.C. Const. Art. V, § 2 cl. (1) & cl. (2). " 'The principles of equality and uniformity are indispensable to taxation, whether general or local. Local taxation must be uniform upon the same class of subjects within the territorial limits of the authority levying the tax, and must be assessed upon all the property according to its just valuation.' " *Hajoca Corp. v. Clayton*, 277 N.C. 560, 569, 178 S.E.2d 481, 487 (1971) (citing Desty on Taxation, Vol 2. p. 1119).

We agree with the Property Tax Commission that the principle of fair, impartial administration of taxation is difficult at best with a contract such as this. Under the terms of the Business Personal Property Audit Agreement, TMA was given the authority to audit "a reasonable sample of the county's business personal property taxpayers." This language appears to give TMA the discretion to choose the sample. Furthermore, the contract compensates TMA at the rate of thirty-five percent of taxes discovered. These two provisions lead to the inescapable conclusion that it would be in TMA's best interest to audit the businesses which own the most property and which conceivably would provide the largest discovery. Clearly, the appearance of potential bias, overreaching, and abuse is substantial.

There is no North Carolina case law on point. In *Sears, Roebuck and Co. v. Parsons*, 260 Ga. 824, 401 S.E.2d 4 (1991), the Georgia Supreme Court examined a contract between a county board of tax assessors and a private auditing company whereby the company was to audit tangible personal property returns as provided by the county's chief assessor. The auditing company was to be paid thirty-five percent of any additional amounts collected as a result of increased valuation as determined by the audit. The board designated Sears, Roebuck and Co. as a taxpayer to be audited under this contract. Sears brought a declaratory judgment action challenging the agreement.

The Georgia Supreme Court held the contract "void as against public policy, not because of the services performed, but because of the contingency scheme of compensation for those services." *Sears*, 401 S.E.2d at 4. The Court reasoned:

> In the exercise of th[e power to tax], the government by necessity acts through its agents. However, this necessity does not require nor authorize the creation of a contractual relationship by which the agent contingently shares in a percentage of the tax collected, and we hold that such an agreement offends public policy. The people's entitlement to fair and impartial tax assessments lies at the heart of our system, and, indeed, was a basic principle upon which this country was founded. Fairness and impartiality are threatened where a private organization has a financial stake in the amount of tax collected as a result of the assessment it recommends.

Id. at 5.

We find *Sears* to be generally on point and the principles applicable here. We believe the present facts to be more egregious to the notion of fair and impartial taxation than in *Sears*, because there the chief assessor determined who would be audited, while here TMA is given the discretion to choose its sample of taxpayers. We are persuaded by the reasoning and holding of *Sears*. While there is no evidence of abuse here, we nevertheless hold that the contingent fee arrangement, which gives TMA a financial stake in the auditing process, gives the appearance of bias and potential abuse and violates public policy.

Philip Morris' cross-appeal argues that the contract and resulting discovery are also violative of its due process and equal protection rights under both the federal and state constitutions. We do not agree. Upon our review of the entire record and the appellant and appellee briefs of

both parties, we conclude that the matters raised and adjudicated in the Commission's Final Decision are not issues of constitutional concern, but are simply issues dealing with the appraisal, listing, or assessment of property. As such, they were properly before the Property Tax Commission, and it is not necessary for us to review the constitutional questions Philip Morris raises in its cross-appeal.

We hold the agreement between Cabarrus County and TMA to be void as against public policy. The Property Tax Commission did not err when it held that the contract itself was null and void as was the discovery that resulted from the contract.

Affirmed.

Chief Judge HEDRICK and Judge WYNN concur.

By Patric P. Wheeler
Deputy Clerk

January 5, 1993

BEFORE THE PROPERTY TAX COMMISSION SITTING AS THE STATE BOARD OF EQUALIZATION AND REVIEW

STATE OF NORTH CAROLINA

COUNTY OF WAKE

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90 PTC 426

FILED MAY 24, 1991

In the matter of:

The appeal of Phillip Morris U.S.A. from the appraisal of certain property by the Cabarrus County Board of Equalization and Review for 1990.

Final Decision

This matter was heard by the Property Tax Commission, sitting as the State Board of Equalization and Review in the City of Raleigh, Wake County, North Carolina on 21 May 1991 pursuant to the appeal of Philip Morris U.S.A. (hereinafter "Taxpayer") from decision of the Cabarrus County Board of Equalization and Review for 1990.

In Paragraph 10 of their Order On Final Pre-hearing Conference (Commission Exhibit 30) filed with the Commission the parties agreed that there were no pending motions, and neither party desired further amendments to the pleadings, except that:

> "the County plans to file motions *in limine* as to (a) evidence on the contentions of Philip Morris U.S.A. with respect to the validity of the contract between Cabarrus County and Tax Management Associates, and (b) evidence concerning a settlement offer made by Philip Morris U.S.A. The taxpayer plans to file motions (a) as to the nullity of the contract between Cabarrus County and Tax Management Associates, (b)

as to the burden of proof, and (c) as to the lack of authority by the County assessor and the Board of Equalization and Review to increase the real property assessment for the years 1989 and 1990. The parties agree that the above motions shall be filed and served no later than 10 May 1991."

As agreed, on 10 May 1991 the Taxpayer filed its "Motion To Declare Discovery Null and Void" and "Motion For An Expedited Decision" (Commission Exhibit 24). Also on 10 May 1991, the County filed its "Motion and Memorandum for ruling on TMA contract issue" (Commission Exhibit 27) and its "Motion and Memorandum On Admissibility of Settlement Negotiations" (Commission Exhibit 28). At the outset of the hearing, the parties asked the Commission to rule on these motions.

After concluding that the matters raised by the Taxpayer in its motions concerning the contract between Tax Management Associates (hereinafter "TMA") and the County were properly before it, the Commission announced the following conclusions of law:

1. The Commission has subject matter jurisdiction to decide all matters, other than constitutional issues, raised by the Taxpayer's and County's motions concerning the contract between TMA and the County, insofar as said contract affects the Taxpayer;

2. Consideration of the contract between TMA and the County for audit services and its effect on the resulting discovery is therefore proper, and the County's motion to exclude the said contract is DENIED.

The Commission then gave the parties an opportunity to offer evidence with regard to the Taxpayer's "Motion To Declare Discovery Null And Void" and "Motion For An Expedited Decision" (Commission Exhibit 24) and the

County's "Motion and Memorandum for ruling on TMA contract issue" (Commission Exhibit 27).

The evidence presented by the Taxpayer and considered by the Commission consisted of the following:

1. Taxpayer Exhibit 1—Business Personal Property Audit Agreement between Cabarrus County and Tax Management Associates, Inc., executed by Terry L. Rowland, Cabarrus County Assessor, on 3 May 1988 and executed by Richard H. Cooke, President of Tax Management Associates, Inc. on 4 May 1988.

The evidence presented by the County and considered by the Commission consisted of the following:

1. County Exhibit 1—Excerpt from the minutes of the Cabarrus County Board of Commissioners (Minute Book 21, pages 11 and 12), approving a budget amendment and accepting the Tax Management Associates, Inc. contract "nunct pro tunct" [sic].
2. County Exhibit 2—Letter from John M. White, Chief Auditor, Tax Management Associates, Inc. to Terry L. Rowland, Cabarrus County Assessor, dated 2 February 1990.
3. County Exhibit 3—Letter from Terry L. Rowland, Cabarrus County Assessor, to James W. Shea, attorney at law, dated 8 May 1990.

COMMISSION EXHIBITS

In addition to the evidence presented by the parties, the Commission also reviewed the following procedural documents:

C-1 Notice of appeal (with attachment), filed 4 December 1990.

C-2 Commission acknowledgement of C-1, 5 December 1990.

C-3 Letter from C. B. McLean, Jr. to David Agosto concerning practice of out-of-state attorneys, 21 December 1990.

C-4 Application For Hearing, filed 3 January 1991.

C-5 *Pro hac vice* Motion, filed 3 January 1991.

C-6 Transmittal letter for C-4 and C-5, filed 3 January 1991.

C-7 Commission acknowledgement of C-4, -5, and -6, 8 January 1991.

C-8 Letter from F. S. Goodrum to James Shea, 25 January 1991.

C-9 Order allowing appearance *pro hac vice*, entered 25 January 1991.

C-10 Letter from C. B. McLean, Jr. to James Shea, 21 February 1991.

C-11 Letter from C. B. McLean, Jr. to James Shea, 4 April 1991.

C-12 Notice of appearance, filed 19 April 1991.

C-13 Transmittal letter for C-12, filed 19 April 1991.

C-14 Motion to compel discovery, filed 22 April 1991.

C-15 Transmittal letter for C-14, filed 22 April 1991.

C-16 Affidavit in opposition to motion to compel discovery, filed 25 April 1991.

C-17 Transmittal letter for C-16, filed 25 April 1991.

C-18 Order compelling discovery in part, entered 1 May 1991.

C-19 Transmittal letter for C-18, 1 May 1991.

C-20 Letter from C. B. McLean, Jr. to David Terry, transmitting subpoena for William Ferris, 7 May 1991.

C-21 Letter from Jean Carter to Commission, transmitting *one* copy of *Taxpayer Exhibit I,* entitled "Asset Listing Setting Forth Acquisition Dates and Detail Costs of All Costs Capitalized For Book (Accounting) Purposes for Each of the Years 1982 through 1988 by Fixed Asset Account Number," filed 10 May 1991.

C-22 Letter from Jean Carter to Commission, transmitting *one* copy of *Taxpayer Exhibit K,* entitled "Asset Listing Setting Forth Each Item of Personal Property Reported by Taxpayer to Cabarrus County in its Personal Property Listings for Each of the Years 1984 through 1989," together with six (6) copies of the Taxpayer's Exhibit Book, filed 10 May 1991.

C-23 Letter from Jean Carter to Commission, transmitting six (6) copies of *Taxpayer Exhibit Z-1,* entitled "Appraisal Report of American Appraisal Associates with respect to Taxpayer's Real Property Located in Cabarrus County," and six (6) copies of *Taxpayer Exhibit Z-2,* entitled "Appraisal Report of American Appraisal Associates with respect to Taxpayer's Personal Property Located in Taxpayer's Cabarrus County Cigarette Manufacturing Facility," filed 10 May 1991.

C-24 "Motion To Declare Discovery Null And Void" and "Motion For An Expedited Decision," filed 10 May 1991.

C-25 Memorandum in Support of "Motion To Declare Discovery Null And Void" and "Motion For An Expedited Decision," filed 10 May 1991.

C-26 Affidavit of Fletcher Hartsell, filed 10 May 1991.

C-27 Cabarrus County's Motion and Memorandum For Ruling on TMA Contract Issue, filed 10 May 1991.

C-28 Cabarrus County's Motion and Memorandum On Admissibility of Settlement Negotiations, filed 10 May 1991.

C-29 Letter from Ms. Arrowwood to Commission, transmitting C-26, -27, and -28, filed 10 May 1991.

C-30 Order On Final Pre-hearing Conference, executed by counsel for the parties, filed 9 May 1991.

C-31 Transmittal letter for C-30, filed 9 May 1991.

C-32 Letter from Mr. Meeker to Commission, requesting subpoena for James F. Wagner, 13 May 1991.

C-33 Subpoena and acknowledgement of service, dated 14 May 1991.

C-34 & C-35 Letters from Mr. Goodrum to the parties, 15 May 1991.

C-36 Hearing Memorandum of Cabarrus County, filed 16 May 1991.

C-37 Transmittal letter for C-36, filed 16 May 1991.

C-38 Transmittal letter for supplemental exhibits filed by Cabarrus County and exhibits A, B, and C to Cabarrus County Exhibit 22, filed 17 May 1991.

C-39 Transmittal letter for Taxpayer Exhibit AA, together with revised Exhibit B and Exhibit D to Pre-hearing Order, filed 17 May 1991.

C-40 Cabarrus County's response to Taxpayer's motion, filed 20 May 1991.

C-41 Hearing Memorandum of Taxpayer, filed 20 May 1991.

FINDINGS OF FACT

After carefully considering the arguments of counsel and the evidence presented by the parties, as listed above, the Commission makes the following Findings of Fact:

1. Taxpayer Exhibit 1 is a contract between TMA and Cabarrus County for audit services.

2. Taxpayer Exhibit 1 was executed by Terry L. Rowland, in his capacity as Cabarrus County Assessor, on or about 3 May 1988.

3. The Cabarrus County Board of Commissioners, in January 1989, "accepted the Tax Management Associates, Inc. contract nunct pro tunct," [sic] as reflected in County Exhibit 1.

4. Taxpayer Exhibit 1 contains the following provisions:

   1. *Services*

   In accordance with the charges, terms, and conditions contained in this agreement, TMA agrees to furnish NCGS (North Carolina General Statutes) audit services on a reasonable sample of the county's business personal property taxpayers. Audits will be performed in compliance with all statutes applicable within the N.C. Machinery Act, specifically: NCGS 105-283, Uniform Appraisal Standards,; NCGS 105-317.1, Appraisal Elements For Reconciling To True Value; and NCGS 105-312, "Discovered Property" Procedures. Customer shall pay all charges due under the schedules in effect.

   2. *Term of Agreement*

   This agreement shall become effective from the date of its acceptance by TMA and shall remain in effect for an initial term of thirty six (36) months and shall continue in effect thereafter on a month-

to-month basis cancellable by either party upon thirty (30) days written notice.

3. *Charges*

For services furnished by TMA under this agreement, customer shall pay to TMA

A. Schedule: 35% of taxes discovered including penalty.

B. Time: 25%—After notice of discovery to taxpayer.
25%—After local appeal right is exhausted.
50%—At time of payment from taxpayer or by last day taxpayer can pay bill without interest, whichever occurs first.

All invoices shall be due and payable in full upon receipt. All amounts not paid within thirty (30) days after date of invoice are subject to a finance charge on the unpaid amount at the rate of one and one-half percent (1-1/2%) per month (annual percentage rate eighteen percent (18%)).

4. *Indemnification*

Customer agrees that proprietary rights to the business personal property audit system shall remain with TMA and that customer will not sell or lease the system to any other person, Company, or taxing jurisdiction or permit access to the system except for employees of the customer authorized to do so by TMA.

5. *General*

The agreement will be governed by the laws of the State of North Carolina.

The customer acknowledges that he has read this

agreement, understands it, and agrees to be bound by its terms and conditions.

6. *Notices*

Notices to be given or submitted by either party to the other, pursuant to this agreement, shall be sufficiently given or made in writing and sent by certified mail, postage prepaid.

5. The discovery by the County conducted against the Taxpayer was a direct result of the County's entry into the agreement with TMA.

CONCLUSIONS OF LAW

Based on its Findings of Fact, as set forth above, the Commission makes the following Conclusions of Law:

1. The Property Tax Commission, sitting as the State Board of Equalization and Review, has the authority to hear and decide appeals concerning the appraisal of the property of public service companies (as defined in G.S. 105-333) and to act as a State board of equalization and review for the valuation and taxation of property in this State, as provided for in G.S. 105-290; see G.S. 143B-222.

2. In its capacity as the State board of equalization and review under G.S. 105-290(a), the Commission is required to hear and adjudicate appeals from boards of county commissioners and from county boards of equalization and review as provided in G.S. 105-290. Under G.S. 105-290(b), the Commission is required to ". . . hear and decide appeals from decisions concerning the listing, appraisal, or assessment of property made by county boards of equalization and review and boards of county commissioners."

3. The Taxpayer made a timely appeal to the Commission from a decision of the Cabarrus County Board of Equalization and Review for 1990. The decision of the said board concerned the listing, appraisal, or assessment of property, and was, under G.S. 105-290, appealable to the Commission.

4. The Commission rejects the County's argument that the contract between TMA and the County is entirely beyond the Commission's subject matter jurisdiction. The Commission concludes as a matter of law that, as the State board of equalization and review, this Commission has not only the authority, but the *duty* to rule upon all issues concerning the listing, appraisal, and assessment of property, except those of constitutional law, properly raised by parties to appeals before it. This includes questions such as the one presented here. The Commission's duty to make such rulings has been recognized by our appellate courts; *see In re McElwee,* 304 N.C. 68, 85, 283 S.E.2d 115, 126 (1981); *see also King v. Baldwin,* 276 N.C. 316, 172 S.E.2d 12 (1970); *see generally Johnston v. Gaston County,* 71 N.C. App. 707, 323 S.E.2d 381 (1984), cert. denied 313 N.C. 508, 329 S.E.2d 392 (1985). In *McElwee,* the Court noted that the "[f]ailure of the Property Tax Commission to recognize the arbitrary and capricious approach taken by the county in this instance was, in itself, arbitrary . . . ." It would be arbitrary for the Property Tax Commission to fail to address the public policy issues regarding the fair, impartial, and uniform listing, appraisal, or assessment of property raised by the Taxpayer in this case.

5. The Commission concludes as a matter of law that the contract between TMA and the County was void as against public policy from its inception because its terms, particularly those contained in paragraph 3, "Charges", so offended conventional

standards requiring fair, impartial, and uniform treatment of this State's taxpayers that it could not stand. The fundamental rule of our system of property taxation is that the tax will be administered in a fair, impartial, and uniform manner, without regard to the identity of the property owed. This principle cannot be followed where a county enters into a contract such as the one presented here. The most recent case involving individuals or organizations having a financial interest in the assessment of property tax or the amount collected is *Sears, Roebuck and Co. v. Parsons,* Case No. S90A1678, decided 21 February 1991. In that case, the Georgia Supreme Court stated "[t]he people's entitlement to fair and impartial tax assessments lies at the heart of our system, and, indeed, was a basic principle upon which this country was founded. Fairness and impartiality are threatened where a private organization has a financial stake in the amount of tax collected as a result of the assessment it recommends."

6. The Commission concludes that the County's attempt to "discover" the Taxpayer's property under the provisions of G.S. 105-312 was void because it resulted directly from the County's entry into a contract that was void as against public policy. The Commission notes that the County is not precluded from initiating a proper discovery under North Carolina General Statute 105-312 with regard to any tax years still within the reach of that statute.

Our system of taxation and collection in this State as well as throughout the nation is based on a program of voluntary compliance. This Commission agrees with the premise that the audit of property tax returns is essential to the enforcement of our voluntary assessment system. However, any voluntary tax compliance system to properly

work must be based on fairness, impartiality and uniformity.

While this decision is based solely upon the examination by the Commission of the facts before it, and does not purport to speak to the public policy aspects of any contract not before it, it is the opinion of the Commission that sound tax policy is not served where individuals or organizations have a financial interest in the assessment of property tax or the amount collected. The implementation of such an enforcement program can only lead to abuses in the enforcement system or at the very least, the appearance to the public of such abuses.

If the essential elements of fairness, impartiality and uniformity are lost in the assessment and collection of property taxes, the underpinning of a voluntary tax system will be weakened and all the people of North Carolina will suffer. While the Commission recognizes that this decision may cause concern among those counties that utilize the services of firms such as was involved in this case, the implementation and administration of a uniform fair and impartial tax assessment and collection system is of paramount importance to the well being of all of the citizens of the State of North Carolina. Public policy must establish and protect such a system and in this case we believe the policy was violated by a system or procedure that invites abuse by private auditors and distrust by taxpayers.

Having decided the case on the basis of public policy, the Commission does not reach the remaining issues raised by the Taxpayer's and the County's motions.

WHEREFORE, IT IS ORDERED, ADJUDGED, AND DECREED THAT the "discovery" of the Taxpayer's property conducted by Cabarrus County is null and void; the County is instructed to revise its tax records as may be necessary to reflect the findings and conclusions of the Commission set forth herein.

Entered this the 24th day of May, 1991.

NORTH CAROLINA PROPERTY TAX COMMISSION

/s/ William P. Pinna
William P. Pinna, Chairman

Commission Member Clarence E. Leatherman and Member John A. Cocklereece, Jr. respectfully dissent from this decision.

Attest:

/s/ Frank S. Goodrum
Frank S. Goodrum, Secretary

Commission Member John A. Cocklereece, Jr. dissenting:

I agree that the contingent fee contract is properly before the Commission. I agree that the Commission has jurisdiction to determine the issue of whether this contract in particular, or another arrangement, contravenes public policy. I respectfully dissent, however, in the Commission's conclusion that the contingent fee arrangement in issue here is, and similar arrangements, because of a contingent payment scheme, may be, void as against public policy.

Whether an arrangement contravenes public policy is not a black and white question. By definition, public policy questions involve a balancing of interests for and against a particular position. In this case the taxpayer argues that contingent fee contracts between counties and auditors contravene public policy because, among other things, they discourage *bona fide* settlement negotiations, and fairness and impartiality in tax administration are threatened. The County argues that such contracts do not contravene public policy because, among other things, the assessor, not the contingent fee auditor, makes the assessment and negotiates settlements, and such contracts are an efficient means of correctly assessing taxpayers in days of constrained budgets. Having balanced the parties respective interests, I do not believe the contingent fee contract in issue here is void as against public policy. Nor do I believe that any similar arrangement, because of its contingent fee payment scheme, is void as against public policy.

While I sympathize with the Taxpayer's arguments as to the dangers of contingent fee contracts, I believe their arguments are best addressed to the legislature, which may establish as a matter of law that contingent fee contracts contravene public policy.

Commission Member Clarence E. Leatherman joins in this dissent.

Decision of the Board of Equalization and Review for Cabarrus County

CABARRUS COUNTY
Post Office Box 707
Concord, North Carolina 28026-0707

November 7, 1990

Mr. James W. Shea
Hunton & Williams
100 Park Avenue
New York, New York 10017

Re: Philip Morris U.S.A.—Property Tax Appeal
Board of Equalization and Review

Dear Mr. Shea:

The Board of Equalization and Review for Cabarrus County reviewed your appeal regarding the proposed discovery of Philip Morris U.S.A. on November 6, 1990.

A motion was made, seconded, and unanimously approved that the proposed discovery of Philip Morris U.S.A. in the amount of $923,339,510 be reduced to $599,426,934.

This adjustment represents, for tax years 1984 through 1989, a total personal property value of $548,499,052, and for tax years 1989 and 1990, a total real property value of $50,927,882.

A ten percent (10%) across the board late listing penalty was recommended and approved for the personal property assessment only.

I have enclosed computations of taxes and penalty resulting in this decision. Also enclosed is computations of the personal property assessment (with and without capitalized interest). Capitalized interest in the amount of $246,284,520 was *excluded* in this assessment.

The real property assessment ($25,463,941 each year) represents HVAC and approximately twenty percent (20%) of the steam, distributed through the Central Power Plant,

for people comfort. This was reclassified as real property and *includes* a capitalized interest value of $5,019,591.

After review of the enclosed material, please advise this office if you desire additional information to explain in greater detail the specifics of the Board of Equalization and Review's decision. If a conference is desired, we will honor that request.

You may within thirty (30) days from the date of this notice file a written notice of appeal and a written statement of the grounds of appeal with the Clerk of the Board of County Commissioners, P.O. Box 707, Concord, N.C. 28026-0707 and with the North Carolina Property Tax Commission, P.O. Box 25000, Raleigh, N.C. 27640.

Sincerely,

Cabarrus County Board of
Equalization and Review

/s/ Terry L. Rowland
Terry L. Rowland
Secretary

Enclosures

Taxes and penalty resulting in 1990 Board of Equalization and Review decision for Philip Morris, U.S.A.

Personal Property

Tax Year	Valuation	Tax Rate	Tax	Penalty	Total Tax
1989	54,178,381	$ .63	$ 341,324.	$ 34,132.	$ 375,456.
1988	78,477,415	.595	466,941.	46,694.	513,635.
1987	91,646,172	.54	494,889.	49,489.	544,378.
1986	100,036,145	.52	520,188.	52,019.	572,207.
1985	108,250,437	.52	562,902.	56,290.	619,192.
1984	115,910,503		602,735.	60,274.	663,009.
	548,499,052		$2,988,979.	$298,898.	$3,287,877.

Real Property

1990	25,463,941	.63	160,423.	—	$ 160,423.
1989	25,463,941	.63	160,423.	—	160,423.
	50,927,882		$320,846.		$320,846.
	599,426,934		$3,309,825.	$298,898.	$3,608,723.

[Accompanying Schedules Omitted]

Final Decision of Respondent's Assessor

CABARRUS COUNTY
Post Office Box 707
Concord, North Carolina 28026-0707

May 8, 1990

Mr. James W. Shea
Hunton & Williams
100 Park Avenue
New York, New York 10017

RE: Philip Morris U.S.A.
Cabarrus County Property Taxes

Dear Mr. Shea:

In accordance with the provisions of North Carolina General Statute 105-312, this is to advise you of the final decision regarding the discovery of property subject to ad valorem taxation in Cabarrus County as described in our notice to you dated December 20, 1989.
A summary of events that have taken place covering this matter is as follows:

December 20, 1989—Letter from Terry L. Rowland, Cabarrus County Assessor, to James W. Shea, Hunton & Williams, Attorneys, legal counsel for Philip Morris, Inc., which constitutes the notice of proposed discovery as provided by North Carolina General Statute 105-312 (d).

January 12, 1990—Letter from James W. Shea to Terry L. Rowland representing a written exception to the proposed discovery in compliance with the provisions of General Statute 105-312 (d)(4).

February 19, 1990—Meeting of the Cabarrus County Board of Commissioners in executive session with Mr. Newton O. Fowler for the purposes of discussion of issues in this matter.

March 7, 1990—Letter from Fletcher L. Hartsell, Jr., Hartsell, Hartsell & Mills, Attorneys, Cabarrus County attorney, to James W. Shea in response to letter to Terry L. Rowland dated January 12, 1990 and Newton Fowler's meeting with the Board of Commissioners of February 19, 1990.

March 21, 1990—Letter from Fletcher L. Hartsell, Jr. to James W. Shea confirming recent discussions, enclosing preliminary audit report from Tax Management Associates and confirming conference scheduled for March 27, 1990 to discuss issues in this matter.

March 27, 1990—Conference with Philip Morris, Inc. representatives, County Assessor, County Manager, consultants, and attorneys representing both parties, for the purpose of presenting evidence or argument regarding the proposed discovery.

April 30, 1990—Letter from William R. McGee, taxpayer consultant, to Mr. John M. White, county consultant, regarding an analysis of Real versus Personal Property which is an issue in this matter.

In addition to the above specified events, there has been a number of telephone conversations and informal discussions that have taken place in regard to the proposed discovery. As a result of all the information which has been submitted and reviewed by both parties, adjustments have been made to amend the proposed discovery as follows:

Tax Year	*Amount	Penalty
1989	$102,544,283	10%
1988	130,267,023	20%
1987	149,470,200	30%
1986	164,730,865	40%
1985	183,322,490	50%
1984	193,004,649	60%

*See Schedule "D" and attached schedules for details.

This revised notice of discovery is being furnished to you in compliance with the provisions of General Statute 105-312 (d). If you desire to take exception to this revised discovery, you must make a written request for review of the Assessor's decision by the Cabarrus County Board of Equalization and Review within fifteen (15) days from the date of this notice. Written request must be directed to the County Assessor as provided by General Statute 105-312 (d).

Cabarrus County continues to recognize a legal and moral obligation to be fair and equitable to all its citizens and through the appeals process, the Cabarrus County taxing officials will continue to work with Philip Morris and its representative in any way possible to bring about a fair and equitable conclusion. We remain prepared to meet with a desire to resolve this matter if possible at any time within the next fifteen days.

Sincerely yours,

/s/ Terry L. Rowland
Terry L. Rowland
Assessor

[Accompanying Schedules Omitted]

Proposed Discovery of Respondent's Assessor

CABARRUS COUNTY
Post Office Box 707
Concord, North Carolina 28026-0707

December 20, 1989

Mr. James W. Shea
Hunton & Williams
100 Park Avenue
New York, New York 10017

Dear Mr. Shea:

Thank you and other Philip Morris, Inc. representatives for meeting with our auditors, Tax Management Associates, Inc. (TMA) and Cabarrus County on December 18 and 19, 1989. We feel the support documentation we requested, and you provided, along with the technical discussion concerning this information, has defined for all parties the resulting discrepancies.

As you are well aware of, the most critical issue is the difference of opinion as to whether the property in question is real or personal property as defined in the North Carolina General Statues. For reasons explained in our meetings, our opinion remains that the subject property is personal property and is administered in a likewise fashion throughout the State of North Carolina. We have received favorable comments on our position from the North Carolina Department of Revenue (Ad Valorem Tax Section), and welcome you to contact their personnel if you so desire.

TMA has indicated to this county that you have provided most of the documentation necessary to complete this audit, and we certainly appreciate your cooperation, time, and effort. I understand you may summit a more detailed account (line item) for expenses incurred for machinery, equipment, and possibly construction in progress. This additional information would be annalized for the purpose of classifying this property as real or personal.

According to the information we have received to date, and pursuant to North Carolina G.S. 105-312, we propose to make the following discovery:

Tax Year	M&E-F&F	CIP	Penalty
1989	$175,000,000	$25,000,000	10%
1988	175,000,000	25,000,000	20%
1987	175,000,000	25,000,000	30%
1986	175,000,000	25,000,000	40%
1985	175,000,000	25,000,000	50%
1984	175,000,000	25,000,000	60%
1983	100,000,000	25,000,000	60%

Enclosed are copies of Business Personal Property returns relating to the above discovery.

These values and penalties will become final unless we receive written exception thereto within thirty (30) days from the date of this letter.

Sincerely,

/s/ Terry L. Rowland
Terry L. Rowland

SUPREME COURT OF NORTH CAROLINA
CHRISTIE SPEIR CAMERON, Clerk
Justice Building, 2 E. Morgan Street
Raleigh, N.C. 27601
(919) 733-3723

23 December 1993

Mr. William S. Patterson
Attorney at Law
Hunton & Williams
One Hanover Square
Suite 1400
Raleigh, NC 27602

Re: The Appeal of Phillip Morris
No. 49PA93

Dear Mr. Patterson:

Motion by Philip Morris to Alter, Amend, or Modify Opinion filed on December 3, 1993; to Shorten Cabarrus County's Time to Respond to this Motion; and for an Expedited Decision has been filed and the following order entered:

"Motion Denied by order of the Court in conference this the 22nd day of December 1993.

s/ Parker, J.
For the Court"

Very truly yours,

Christie Speir Cameron
Clerk of Supreme Court

/s/ Peggy N. Byrd
Peggy N. Byrd
Assistant Clerk

NORTH CAROLINA COURT OF APPEALS

NO: 93PTC496M-PC
County: PROP. TAX COMM.
Number: 90-PTC-426

FILED 10 JANUARY 1994

ORDER

The following Order was entered:

"The petition and motion filed in this cause on the 23rd dat [sic] if [sic] December, 1993 and designated "Philip Morris U.S.A.'s Motion Under Appellate Rule 2 to Suspend or Vary the Rules, or, Alternatively, Philip Morris U.S.A.'s Petition for Writ of Certiorari Under Appellate Rule 21" are Denied.

By order of the Court this 7th day of January, 1994."

The above order is therefore certified to the North Carolina Property Tax Commission.

Witness my hand and official seal this the 10th day of January, 1994.

/s/ John H. Connell
Clerk of the Court of Appeals

SUPREME COURT OF NORTH CAROLINA
TENTH DISTRICT

No. 49PA93

From NC Court of Appeals
(9110PTC762)
From Property Tax Commission
(90PTC426)

In the Matter of:
The Appeal of Philip Morris U.S.A. from the decision of the Cabarrus County Board of Equalization and Review for personal property taxes years 1984-1989

(appealed by Cabarrus County)
FILED FEBRUARY 3, 1994
ORDER

Upon consideration of the petition filed by Philip Morris in this matter for rehearing of the decision of this Court pursuant to Rule 31, N.C. Rules of Appellate Procedure, the following order was entered and is hereby certified to the North Carolina Court of Appeals:

"Denied by order of the Court in conference, this the 27th day of January 1994.

/s Parker, J.
For the Court"

WITNESS my hand and the seal of the Supreme Court of North Carolina, this the 3rd day of February 1994.

Christie Spair Cameron
Clerk, Supreme Court of North Carolina
/s/ Peggy N. Byrd
Peggy N. Byrd
Assistant Clerk

GENERAL STATUTES OF NORTH CAROLINA

Excerpts from
Chapter 105

Taxation

NOVEMBER 1992

§ 105-273. Definitions.

When used in this Subchapter (unless the context requires a different meaning):

* * *

(6a) "Discovered property" includes all of the following:

a. Property that was not listed during a listing period.

b. Property that was listed but the listing included a substantial understatement.

c. Property that has been granted an exemption or exclusion and does not qualify for the exemption or exclusion.

(6b) "To discover property" means to determine any of the following:

a. Property has not been listed during a listing period.

b. A taxpayer made a substantial understatement of listed property.

c. Property was granted an exemption or exclusion and the property does not qualify for an exemption or exclusion.

* * * *

§ 105-283. Uniform appraisal standards.

All property, real and personal, shall as far as practicable be appraised or valued at its true value in money. When used in this Subchapter, the words "true value" shall be interpreted as meaning market value, that is, the price estimated in terms of money at which the property would change hands between a willing and financially able buyer and a willing seller, neither being under any compulsion to buy or to sell and both having reasonable knowledge of all the uses to which the property is adapted and for which it is capable of being used. For the purposes of this section, the acquisition of an interest in land by an entity having the power of eminent domain with respect to the interest acquired shall not be considered competent evidence of the true value in money of comparable land.

* * * *

§ 105-296. Powers and duties of assessor.

(a) The county assessor shall have general charge of the listing, appraisal, and assessment of all property in the county in accordance with the provisions of law. He shall perform the duties imposed upon him by law, and he shall have and exercise all powers reasonably necessary in the performance of his duties not inconsistent with the Constitution or the laws of this State.

(b) Within budgeted appropriations, he shall employ listers, appraisers, and clerical assistants necessary to carry out the listing, appraisal, assessing, and billing functions required by law. The assessor may allocate responsibility among such employees by territory, by subject matter, or

on any other reasonable basis. Each person employed by the assessor as a real property appraiser or personal property appraiser shall during the first year of employment and at least every other year thereafter attend a course of instruction in his area of work. At the end of the first year of their employment, such persons shall also achieve a passing score on a comprehensive examination in property tax administration conducted by the Department of Revenue.

* * *

(g) He shall have power to subpoena any person for examination under oath and to subpoena documents whenever he has reasonable grounds for the belief that such person has knowledge or that such documents contain information that is pertinent to the discovery or valuation of any property subject to taxation in the county or that is necessary for compliance with the requirements as to what the tax list shall contain. The subpoena shall be signed by the chairman of the board of equalization and review if that board is in session; otherwise, it shall be signed by the chairman of the board of county commissioners. It shall be served by an officer qualified to serve subpoenas. Any person who shall wilfully fail or refuse to appear, produce subpoenaed documents, or testify concerning the subject of the inquiry shall be guilty of a misdemeanor and fined and/or imprisoned in the discretion of the court.

(h) Only after the abstract has been carefully reviewed can the assessor require any person operating a business enterprise in the county to submit a detailed inventory, statement of assets and liabilities, or other similar information pertinent to the discovery or appraisal of property taxable in the county. Inventories, statements of assets and liabilities, or other information secured by the assessor under the terms of this subsection, but not expressly required by this Subchapter to be shown on the abstract itself, shall not be open to public inspection but shall be

made available, upon request, to representatives of the Department of Revenue or of the Employment Security Commission. Any assessor or other official or employee disclosing information so obtained, except as may be necessary in listing or appraising property in the performance of official duties, or in the administrative or judicial proceedings relating to listing, appraising, or other official duties, shall be guilty of a misdemeanor and punishable by a fine not exceeding fifty dollars ($50.00).

* * * *

§ 105-299. Employment of experts.

The board of county commissioners may employ appraisal firms, mapping firms or other persons or firms having expertise in one or more of the duties of the assessor to assist him or her in the performance of such duties. The county may make available to such persons any information it has that will facilitate the performance of a contract entered into pursuant to this section. Persons receiving such information shall be subject to the provisions of G.S. 105-289(e) and G.S. 105-259 regarding the use and disclosure of information provided to them by the county. Any person employed by an appraisal firm whose duties include the appraisal of property for the county shall be required to demonstrate that he or she is qualified to carry out such duties by achieving a passing grade on a comprehensive examination in the appraisal of property administered by the Department of Revenue. In the employment of such firms, primary consideration shall be given to the firms registered with the Department of Revenue pursuant to the provisions of G.S. 105-289(i). A copy of the specifications to be submitted to potential bidders and a copy of the proposed contract may be sent by the board to the Department of Revenue for review before the invitation or acceptance of any bids. Contracts for the employment of such firms or persons shall be deemed to be contracts for personal services and shall not be subject

to the provisions of Article 8, Chapter 143, of the General Statutes.

* * * *

§ 105-312. (Effective until January 1, 1993) Discovered property; appraisal; penalty.

* * *

(b) Duty to Discover and Assess Unlisted Property.—It shall be the duty of the assessor to see that all property not properly listed during the regular listing period be listed, assessed and taxed as provided in this Subchapter. The assessor shall file reports of such discoveries with the board of commissioners in such manner as the board may require.

* * *

(d) Procedure for Listing, Appraising, and Assessing Discovered Property.—Subject to the provisions of subsection (c), above, and the presumptions established by subsection (f), below, discovered property shall be listed by the assessor in the name of the person required by G.S. 105-302 or G.S. 105-306. The discovery shall be deemed to be made on the date that the abstract is made or corrected pursuant to subsection (e) of this section. The assessor shall also make a tentative appraisal of the discovered property in accodance with the best information available to him.

When a discovery is made, the assessor shall mail a notice to the person in whose name the discovered property has been listed. The notice shall contain the following information:

(1) The name and address of the person in whose name the property is listed;

(2) A brief description of the property;

(3) A tentative appraisal of the property;

(4) A statement to the effect that the listing and appraisal will become final unless written exception thereto is filed with the assessor within 30 days from date of the notice.

Upon receipt of a timely exception to the notice of discovery, the assessor shall arrange a conference with the taxpayer to afford him the opportunity to present any evidence or argument he may have regarding the discovery. Within 15 days after the conference, the assessor shall give written notice to the taxpayer of his final decision. Written notice shall not be required, however, if the taxpayer signs an agreement accepting the listing and appraisal. In cases in which agreement is not reached, the taxpayer shall have 15 days from the date of the notice to request review of the decision of the assessor by the board of equalization and review or, if that board is not in session, by the board of commissioners. Unless the request for review by the county board is given at the conference, it shall be made in writing to the assessor. Upon receipt of a timely request for review, the provisions of G.S. 105-322 or G.S. 105-325, as appropriate, shall be followed.

* * *

(g) Taxation of Discovered Property.—When property is discovered, it shall be taxed for the year in which discovered and for any of the preceding five years during which it escaped taxation in accordance with the assessed value it should have been assigned in each of the years for which it is to be taxed and the rate of tax imposed in each such year. The penalties prescribed by subsections (h) and (h1) of this section shall be computed and imposed regardless of the name in which the discovered property is listed. If the discovery is based upon an understatement of value, quantity, or other measurement rather than an omission from the tax list, the tax shall be computed on the ad-

ditional valuation fixed upon the property, and the penalties prescribed by subsections (h) and (h1) of this section shall be computed on the basis of the additional tax.

* * * *

§ 105-312. (Effective January 1, 1993) Discovered property; appraisal; penalty.

* * *

(b) Duty to Discover and Assess Unlisted t shall be the duty of the assessor to see that all property not properly listed during the regular listing period be listed, assessed and taxed as provided in this Subchapter. The assessor shall file reports of such discoveries with the board of commissioners in such manner as the board may require.

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(1) The name and address of the person in whose name the property is listed;

(2) A brief description of the property;

(3) A tentative appraisal of the property;

(4) A statement to the effect that the listing and appraisal will become final unless written exception thereto is filed with the assessor within 30 days from date of the notice.

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* * *

(g) Taxation of Discovered Property.—When property is discovered, it shall be taxed for the year in which discovered and for any of the preceding five years during which it escaped taxation in accordance with the assessed value it should have been assigned in each of the years for which it is to be taxed and the rate of tax imposed in each such year. The penalties prescribed by subsection (h) of this section shall be computed and imposed regardless of the name in which the discovered property is listed. If the discovery is based upon an understatement of value, quantity, or other measurement rather than an omission from

the tax list, the tax shall be computed on the additional valuation fixed upon the property, and the penalties prescribed by subsection (h) of this section shall be computed on the basis of the additional tax.

* * * *

§ 105-322. County board of equalization and review.

* * *

(g)(1) Powers and Duties.—It shall be the duty of the board of equalization and review to examine and review the tax lists of the county for the current year to the end that all taxable property shall be listed on the abstracts and tax records of the county and appraised according to the standard required by G.S. 105-283, and the board shall correct the abstracts and tax records to conform to the provisions of this Subchapter. In carrying out its responsibilities under this subdivision (g)(1), the board, on its own motion or on sufficient cause shown by any person, shall:

a. List, appraise, and assess any taxable real or personal property that has been omitted from the tax lists.

b. Correct all errors in the names of persons and in the description of properties subject to taxation.

c. Increase or reduce the appraised value of any property that, in the board's opinion, shall have been listed and appraised at a figure that is below or above the appraisal required by G.S. 105-283; however, the board shall not change the appraised value of any real property from that at which it was appraised for the preceding year

except in accordance with the terms of G.S. 105-286 and 105-287.

d. Cause to be done whatever else shall be necessary to make the lists and tax records comply with the provisions of this Subchapter.

e. Embody actions taken under the provisions of subdivisions (g)(1)a through (g)(1)d, above, in appropriate orders and have the orders entered in the minutes of the board.

f. Give written notice to the taxpayer at his last-known address in the event the board shall, by appropriate order, increase the appraisal of any property or list for taxation any property omitted from the tax lists under the provisions of this subdivision (g)(1).

(2) On request, the board of equalization and review shall hear any taxpayer who owns or controls property taxable in the county with respect to the listing or appraisal of his property or the property of others.

a. A request for a hearing under this subdivision (g)(2) shall be made in writing to or by personal appearance before the board prior to its adjournment. However, if the taxpayer requests review of a decision made by the board under the provisions of subdivision (g)(1), above, notice of which was mailed fewer than 15 days prior to the board's adjournment, the request for a hearing thereon may be made within 15 days after the notice of the board's decision was mailed.

b. Taxpayers may file separate or joint requests for hearings under the provisions of this subdivision (g)(2) at their election.

c. At a hearing under provisions of this subdivision (g)(2), the board, in addition to the powers it

may exercise under the provisions of subdivision (g)(3), below, shall hear any evidence offered by the appellant, the assessor, and other county officials that is pertinent to the decision of the appeal. Upon the request of an appellant, the board shall subpoena witnesses or documents if there is a reasonable basis for believing that the witnesses have or the documents contain information pertinent to the decision of the appeal.

d. On the basis of its decision after any hearing conducted under this subdivision (g)(2), the board shall adopt and have entered in its minutes an order reducing, increasing, or confirming the appraisal appealed or listing or removing from the tax lists the property whose omission or listing has been appealed. The board shall notify the appellant by mail as to the action taken on his appeal not later than 30 days after the board's adjournment.

(3) In the performance of its duties under subdivisions (g)(1) and (g)(2), above, the board of equalization and review may exercise the following powers:

a. It may appoint committees composed of its own members or other persons to assist it in making investigations necessary to its work. It may also employ expert appraisers in its discretion. The expense of the employment of committees or appraisers shall be borne by the county. The board may, in its discretion, require the taxpayer to reimburse the county for the cost of any appraisal by experts demanded by him if the appraisal does not result in material reduction of the valuation of the property appraised and if the appraisal is not subsequently reduced materially by the board or by the Department of Revenue.

b. The board, in its discretion, may examine any witnesses and documents. It may place any witnesses under oath administered by any member of the board. It may subpoena witnesses or documents on its own motion, and it must do so when a request is made under the provisions of subdivision (g)(2)c, above.

A subpoena issued by the board shall be signed by the chairman of the board, directed to the witness or to the person having custody of the document, and served by an officer authorized to serve subpoenas. Any person who willfully fails to appear or to produce documents in response to a subpoena or to testify when appearing in response to a subpoena shall be guilty of a misdemeanor and punished by a fine or by imprisonment or by both in the discretion of the court.

(4) Upon the completion of its other duties, the board may submit to the Department of Revenue a report outlining the quality of the reappraisal, any problems it encountered in the reappraisal process, the number of appeals submitted to the board and to the Property Tax Commission, the success rate of the appeals submitted, and the name of the firm that conducted the reappraisal. A copy of the report should be sent by the board to the firm that conducted the reappraisal.

TAX MANAGEMENT ASSOCIATES, INC.
BUSINESS PERSONAL PROPERTY AUDIT AGREEMENT
TMA AGREEMENT NO. B.P.

Between *CABARRUS*

(Herein after called "customer"), and Tax Management, Associates, Inc. (herein after called "TMA".) a corporation authorized to transact business in North Carolina and having its principal place of business in Charlotte, North Carolina.

GENERAL TERMS AND CONDITIONS

1. SERVICES

In accordance with the charges, terms and conditions contained in this agreement, TMA agrees to furnish NCGS (North Carolina General Statutes) audit services on a reasonable sample of the County's business personal property taxpayers. Audits will be performed in compliance with all statutes applicable within the N.C. Machinery Act, specifically; NCGS 105-283, Uniform Appraisal Standards; NCGS 105-317.1, Appraisal Elements for Reconciling to True Value; and NCGS 105-312, "Discovered Property" Procedures. Customer, shall receive two (2) copies of valuation report in the format agreed upon. Customer shall pay all charges due under the schedules in effect.

2. TERM OF AGREEMENT

This Agreement shall become effective from the date of its acceptance by TMA and shall remain in effect for an initial term of thirty six (36) months and shall continue in effect thereafter on a month-to-month basis cancellable by either party upon thirty (30) days written notice.

3. CHARGES

For services furnished by TMA under this Agreement, customer shall pay to TMA:

A. Schedule: 35% of taxes discovered including penalty.

B. Time: 25%—After notice of discovery to taxpayer
25%—After local appeal right is exhausted.
50%—At time of payment from taxpayer or by last day taxpayer can pay bill without interest, whichever occurs first.

All invoices shall be due and payable in full upon receipt. All amounts not paid within thirty (30) days after date of invoice are subject to a finance charge on the unpaid amount at the rate of one and one-half percent (1-1/2%) per month (annual percentage rate eighteen percent (18%)).

4. INDEMNIFICATION

Customer agrees that proprietary rights to the business personal property audit system shall remain with TMA and that customer will not sell or lease the system to any other person, company, or taxing jurisdiction or permit access to the system except for employees of the customer authorized to do so by TMA.

5. GENERAL

The Agreement will be governed by the laws of the State of North Carolina.

The customer acknowledges that he has read this agreement, understands it, and agrees to be bound by its terms and conditions.

6. NOTICES

Notices to be given or submitted by either party to the other, pursuant to this agreement, shall be sufficiently given or made in writing and sent by certified mail, postage prepaid.

ACCEPTED: TAX MANAGEMENT ASSOCIATES, INC.
Authorized Signature: /s/ Richard H. Cooke
Name: Richard H. Cooke

Title: President
Date: 5/4/88

ACCEPTED: CABARRUS COUNTY
Authorized Signature: /s/ Terry L. Rowland
Name: Terry L. Rowland
Title: Assessor
Date: May 3, 1988

CABARRUS COUNTY
Post Office Box 707
Concord, North Carolina 28026-0707

September 19, 1989

Mr. C.A. Saulo, Tax Manager
Philip Morris, Inc.
120 Park Avenue
New York, New York 10017

Dear Mr. Saulo:

Our auditors have advised they were unable to complete their audit when they visited your offices on August 24th in New York.

Over the past nine (9) months we believe our auditors have made every possible effort to secure the data and complete this audit in a formal way. However, only a limited amount of accounting records for fixed assets and inventory have been made available. Being the excellent corporate citizen you are, and our number one (1) taxpayer, this has caused us much concern.

Based on their report, which contains estimates due to lack of information, we propose to make the following discoveries pursuant to North Carolina General Statue [sic] 105-312:

Tax Year	M&E-F&F	CIP	Penalty
1989	$100,000,000	$25,000,000	10%
1988	100,000,000	25,000,000	20%
1987	100,000,000	25,000,000	30%
1986	100,000,000	25,000,000	40%
1985	100,000,000	25,000,000	50%
1984	100,000,000	25,000,000	60%
1983	100,000,000	25,000,000	60%

It is our desire to be fair and equitable with all taxpayers in Cabarrus County. We have conducted over one hundred

and fifty (150) audits within the past year with the proper records made available upon our request. We feel this County has been fair and patient with Philip Morris, Inc.

Our final request is any information or records that you possess that can change the above proposed assessment should be supplied to our auditors by Friday, October 6, 1989.

These values and penalties will become final unless we receive written exception thereto within thirty (30) days from the date of this letter.

Sincerely,

/s/ Terry L. Rowland
Terry L. Rowland
Assessor

Tax Management Associates, Inc. P.O. Box 10065
801 Oberlin Road, Suite 200
Raleigh, N.C. 27605-0065
Phone (919) 828-7660 or 825-7836

February 2, 1990

Mr. Terry L. Rowland, Assessor
Cabarrus County Tax Office
Post Office Box 707
Concord, North Carolina 28026-0707

RE: Philip Morris, Inc.
Property Tax Audit
(Preliminary Report to Assessor)

Dear Mr. Rowland:

We have reviewed the data which was furnished by the subject taxpayer relating to the audit of their Business Personal Property Tax Returns for the years 1983 thru 1989, inclusive.

With the information furnished, primarily a "Summary of Fixed Assets by Account, Cabarrus Manufacturing Facility as of December 31, 1988," together with the additional data supplied at the December 18, 1989 meeting, we make the following observations:

1. The "Summary of Fixed Assets by Account, Cabarrus Manufacturing Facility as of December 31, 1988," hereinafter referred to as "Asset Summary", has been verified with and tied to the supplemental schedules furnished at the December 18, 1989 meeting. The values for the assets listed were at full absorbed cost. Construction-in-Progress amounts were not included in the Asset Summary.

2. After making a comprehensive analysis of the Asset Summary it was evident that a substantial understatement existed in the various equipment values which were reported in the Business Property Tax Returns.

3. Inasmuch as the various accounts comprising the Asset Summary contained a mixture of assets that related to other accounts, a complete analysis was made of each account by year acquired. After proper classification of each account was made, the various accounts were adjusted or re-classed accordingly.

4. To support the explanation of re-classification of the Asset Summary, we are attaching the following schedules:

   Schedule "A": Represents the analysis of the Asset Summary based on the document as furnished by the Taxpayer.

   Schedule "B": Represents the analysis of the Asset Summary based on the document as furnished by the Taxpayer after making re-classification adjustments as indicated on Schedules B-305; B-310; B-315; B-320; B-325; B-330 and B-340.

5. Schedule "B" Sub-Accounts contain the re-class and adjusted cost values for the following categories:

   B-305 Land Improvements, account #305
   B-310 Buildings, account #310
   B-315 Building Equipment, account #315
   B-320 Machinery & Equipment, account #320
   B-325 Data Processing Equipment, account #325
   B-330 Furniture & Fixtures, account #330
   B-340 Transportation Equipment, account #340
   B-399 Explanation of re-class notes for the asset accounts itemized above.

6. Schedule "C":

   Represents the total personal property assessed tax values for 1984 thru 1989 for the categories of

assets which include Machinery & Equipment; Furniture and Fixtures; Building Equipment and Data Processing Equipment. It should be noted that the assessed tax value for the Railroad Spur Track which was assessed on the real property card has been added in this schedule since the cost for same has been re-classed from schedule B-305, Land Improvements to Schedule B-320, Machinery & Equipment.

7. Schedule "D":

Represents the total calculated tax values for the adjusted cost values for 1984 thru 1989 from Schedule "B" using the appropriate trending tables utilized by Cabarrus County for establishing tax values as published by the North Carolina Department of Revenue, Ad Valorem Tax Division. The tables used for each category are as follows:

B-15 Machinery & Equipment
E-10 Building Equipment
K-10 Furniture & Fixtures
L-6 Data Processing Equipment

Construction-in-progress is being assessed at 100% of the cost values inasmuch as this equipment has not been placed in service and therefore has not depreciated in value.

8. Schedule "D": (continued)

Also represents the summary of calculated tax values based on the adjusted cost values by category from Schedule "B" and detailed by Schedules B-315; B-320; B-325 and B-330. Construction-in-progress amounts were obtained from the financial statements furnished by the taxpayer. The total assessed values were obtained from the tax returns for each year as per detail from Schedule "C". The total variance in Schedule "D" represents the total

proposed assessment in accordance with North Carolina General Statutes 105-312.

9. Schedule "D" Sub-Accounts represent the detailed calculations by year acquired for each category using the appropriate trending schedules as follows:

   Schedule "D-1" (B-15) Machinery & Equipment
   Schedule "D-2" (E-10) Building Equipment
   Schedule "D-3" (K-10) Furniture & Fixtures
   Schedule "D-4" (L-6) Data Processing Equipment

   Construction-in-progress is being assessed at 100% of the cost values inasmuch as this equipment has not been placed in service and therefore has not depreciated in value.

   The above observations and schedules are presented to inform you of our process used in establishing the cost values of the various classes of personal property detailed in the Asset Summary furnished by the taxpayer. Since the issue of "Real vs Personal" was discussed at length in our December 1989 meeting, we feel that the proper classification of assets contained in the Asset Summary was extremely important. The net result was adjustments in the accounts as presented in the sub-"B" accounts.

During the examination of the Asset Summary, it became apparent that certain areas need to be addressed and resolved with further communication with the taxpayer and/or examination of the tax office records or establish the position of Cabarrus County in making any proposed assessment based on the information contained in this report. These areas are as follows:

1. Spur Track Re-class:

   It was observed from the Land Improvement Account that the total acquired cost of this property was $4,422,446, and acquired in 1982 and

1983. The real property card had a value of $482,944. We have re-classed these costs to account #320, Machinery & Equipment and depreciated accordingly. Credit for the tax value on this property as real, has been provided in the total assessed tax values as per Schedule "C".

2. Computer Software costs:

   This report contains 100% of the acquired costs for this property. You have, as we understand, historically excluded customized software and taxed only packaged software. Inasmuch as we are unable at this point to determine the nature of the software items in the Asset Summary, we have included all such property in this report.

3. Pollution Abatement Equipment:

   This report makes no provision for excluding this equipment inasmuch as no AV-12 Certifications are on file to properly exempt this property. The total amount included herein is $6,663,142 and was acquired over a four (4) year period, 1982 thru 1985.

4. Boiler & Boiler House:

   From our observation of the real property cards, no equipment or buildings for this facility are included with the real property values. We have not included these cost values in our personal property accounts but feel a more thorough examination should be made before any re-classification takes place.

5. Disposals of Equipment:

   The values for all personal property included in this report were obtained from the Asset Summary as of December 31, 1988. No attempt has

been made to add back any equipment that was disposed in any prior years.

6. Assumption:

We have assumed that the Asset Summary as of December 31, 1988 included all assets in Cabarrus County, with the exception of Construction-in-progress, and that they were there since the date acquired. (There appears to be a small amount of assets that were possibly transferred to the Cabarrus Plant from other locations. Although included in this report, we feel that the amount is not material and would more or less be offset by any disposals.)

7. Valuation of Data Processing Equipment:

We have used the L-6 trending schedule to value this equipment from 1984 thru 1989. This equipment was depreciated on an eight (8) year life through 1987 and changed to a six (6) year life in 1988. This was done with your approval to be consistent with the valuation and to correct the prior years in favor of the taxpayer.

8. Real Property:

We have included in our adjustments in Schedules B-310 and B-315 such items as silos, tanks, cooling tower, etc. which appear on the real property cards. Although they appear on the real property cards, there is a substantial difference in the acquired costs with relation to the assessed values. No additional assessment on real property is in this report. Some inspection at the facility on these items by the real estate department maybe necessary to determine if properly assessed.

9. 1983 Tax Year:

No additional assessment is made in this report

for this Tax Year inasmuch as the amounts reported by the taxpayer included substantially all the assets as of December 31, 1982.

10. Construction in Progress:

The amounts made available by the taxpayer for this category did not reveal whether it was Real or Personal Property. Pending receipt of a more descriptive analysis of this account, we have included the entire amount as Personal Property. The basis for this decision is that during the period covered by this audit, the real property accounts increased only $2,850,000. The equipment accounts increased $95,087,000. The total amount of CIP for the tax years included in this report total $88,893,000. For this reason we are including the CIP as personal property pending receipt of additional data from taxpayer.

Based on the examination of the data received and our analysis as per the attached schedules reflecting our approach to establishing the tax values herein, we recommend that the proposed discovery dated December 20, 1989 be amended as follows:

Tax Year	*Amount	Penalty
1989	$109,517,118	10%
1988	137,871,145	20%
1987	157,748,698	30%
1986	174,244,015	40%
1985	193,344,955	50%
1984	203,095,576	60%

*See Schedule "D" for detail

The above amounts represent the depreciated tax values where applicable. I am enclosing herewith fifteen (15) copies of this report for your convenience.

Please advise me of any revisions that you feel need to be made that could change this report. If I can be of any assistance, please call me at (919) 828-7660.

Very truly yours,

/s/ John M. White
John M. White
Chief Auditor

[Accompanying Schedules Omitted]

Hunton & Williams
100 Park Avenue
New York, New York 10017

May 17, 1990

Mr. Terry L. Rowland, Assessor
Cabarrus County
Cabarrus County Courthouse
P.O. Box 707
Concord, N.C. 28026-0707

Re: Philip Morris U.S.A.
Cabarrus County Property Taxes

Dear Mr. Rowland:

In behalf of Philip Morris U.S.A. ("Philip Morris") and in accordance with the provisions of Section 105-312(d), North Carolina General Statutes ("G.S."), I am enclosing the formal request by Philip Morris for review by the Board of Equalization and Review of the final decision dated May 3, 1990.

In light of (i) the conferences attended by you, me, representatives of Tax Management Associates, Inc. ("Tax Management"), representatives of Cabarrus County and representatives of Philip Morris on December 18 and December 19, 1989, March 27, 1990 and May 16, 1990, (ii) the inordinate time and effort expended with respect to the audit and (iii) the substantial expenses incurred by Philip Morris to satisfy the demands of Tax Management during the arduous course of the audit, I am taking the liberty of summarizing our beliefs with respect to this case based on the facts and circumstances we have encountered, examined and evaluated.

We believe that Philip Morris prepared and submitted its North Carolina Personal Property Tax Returns (the "Returns", for the years 1983 through 1989 in substantial compliance with the applicable laws of North Carolina. We further believe that Tax Management utilized appraisal techniques which are in direct violation of the North Car-

olina appraisal and assessment property tax laws. The dollar discrepancies between the amounts reported by Philip Morris on the Returns and the amounts asserted by Tax Management in its proposed discovery as amended in the purported final decision dated May 8, 1990 are essentially attributable to the following two factors:

1. Philip Morris appraised or valued the personal property reported on the Returns at its market value (the price estimated in terms of money at which the property would change hands between a willing and financially able buyer and a willing seller) under Section 105-283, G.S. Tax Management did not appraise or value the property under Section 105-283, G.S. (or any other North Carolina statute) but merely asserted the sum of a) the basis of the property as finally determined for Federal investment tax credit purposes under Section 48 of the Internal Revenue Code (which includes hard costs (purchase price of the property) and any indirect costs however remotely connected to the property and regardless of whether such costs have any affect on the market value of the property), plus b) "book interest", as the value of the personal property in question for North Carolina personal property tax purposes.

2. Substantially all of the building equipment reflected on the books of Philip Morris was properly included by you, as the Assessor, in the real property appraisals and taxed as real property during the years in question. Accordingly, Philip Morris reported on the Returns only those building and equipment assets which Philip Morris verily believed were not included in the real property appraisal. The market value of such building equipment was $4,847,102. On the other hand, Tax Management "discovered" building and equipment assets in the amount of $126,118,925 (this amount also represents the basis of such property as finally determined for Federal investment tax purposes plus book interest and not market value) notwithstanding that substantially all of such building and equipment assets were in fact taxed as real property. In

April, 1990, Strategis Asset Valuation and Management (Philip Morris' appraisal firm) made an extensive examination of the building and equipment asset account and determined that items in this account with a market value of $4,149,400 constituted personal property which should have been reported on the Returns. The appraisal firm also determined that the items of building and equipment reported by Philip Morris on the Returns with a market value of $4,847,102 should not have been reported because they were properly included in the real property appraisals and taxed as real property.

The differences between the amounts reflected on the Returns and the amounts asserted by Tax Management in its "discovery" may be summarized by accounts as follows:

I. Machinery and Equipment

Market Value Per Returns	Federal Investment Tax Credit Value Per Tax Management
$174,680,332	$239,296,468

The difference ($64,616,136) between the market value as shown on the Returns and the Federal investment tax credit value as modified (to include "book interest") and adopted by Tax Management represents book interest in the amount of $36,734,750 and soft costs (indirect costs) which we fully discussed at the May 16, 1990 conference and which we believe do not enhance the value of the assets to which they were allocated for Federal investment tax credit purposes.

II. Building Equipment

Market Value Per Returns	Federal Investment Tax Credit Value Per Tax Management
$4,847,102	$126,118,925

The difference ($121,271,823) between the market value

as shown on the Returns and the Federal investment tax credit value as modified (to include "book interest") and adopted by Tax Management represents book interest in the amount of $29,769,879 and building and equipment assets included in the real property appraisals of the Assessor and subjected to real property taxes during the years under audit.

III. Furniture and Fixtures

Market Value Per Returns	Federal Investment Tax Credit Value Per Tax Management
$4,630,105	$4,724,674

The Federal investment tax credit value as modified (to include "book interest") and adopted by Tax Management includes book interest in the amount of $717,805.

IV. Data Processing Equipment

Market Value Per Returns	Federal Investment Tax Credit Value Per Tax Management
$4,509,039	$5,678,929

The difference ($1,169,890) between the market value as shown on the Returns and the Federal investment tax credit value as modified (to include "book interest") and adopted by Tax Management includes book interest in the amount of $734,839.

The above analysis clearly indicates that:

1. Tax Management is including in its so-called "values" of machinery and equipment (and building equipment) book interest, soft cost and other indirect costs, "booked" by Philip Morris, in the case of: (i) book interest, to comply with generally accepted accounting principles in determining the earnings of Philip Morris, and (ii) soft costs and other indirect costs, for Federal investment tax credit pur-

poses, regardless of the fact that such costs do not enhance the market value of the assets. A flagrant example of this is allocated book interest which not only does not enhance the fair market value of the asset to which it was allocated but is specifically excluded by the North Carolina Department of Revenue as an item to be considered in appraising business personal property.

2. Tax Management is subjecting building and equipment assets (which are classified as such solely for Federal investment tax credit purposes) to personal property taxes even though such assets were clearly in the real property appraisals of the Assessor and subjected to real property taxes. It should be especially noted that Tax Management is devoid of knowledge in the real property appraisal field and is totally indifferent to the "double taxation" being imposed upon Philip Morris.

At the meeting held in your office on May 16, 1990, Tax Management proposed to add the following Federal investment tax credit cost items to the market values of the machinery and equipment as shown on the Returns:

Machinery Installation	($5,969,376)
Stacker Crane Installation	(2,818,165)
Carton/Case Installation	(178,745)
JES Eng. Fees	(8,489,688)
P.M. Overhead	(2,628,210)
CTB-Eng. Fees	(499,800)

We agreed to the increase in the market values of machinery and equipment as shown on the Returns with respect to installation costs and are reviewing the JES Eng. Fees, P.M. Overhead and CTB-Eng. Fees to determine the extent, if any, to which these costs are included in the building accounts and real property appraisals.

The Tax Management allegations of omissions by Philip Morris with respect to the building and equipment assets are staggering at best. In order to address the civil nature

of these allegations we have agreed to a meeting in your offices to be held on May 24, 1990 at 9:00 A.M. and to be attended by you, me and Messrs. John Paterson, William McGee, Dennis Parker and John White. I believe that at the conclusion of this meeting all parties should be better situated to assess and assert their positions and, if necessary, pursue their grievances.

Sincerely,

/s/ James W. Shea
James W. Shea

JWS:cas
Encls.

SUPREME COURT OF NORTH CAROLINA

No. 49PA93

In the Matter of:

The Appeal of Philip Morris U.S.A. from the decision of the Cabarrus County Board of Equalization and Review for personal property taxes years 1984-1989

Excerpts from
NEW BRIEF OF APPELLEE
PHILIP MORRIS U.S.A.

FILED
1993 MAY 17
From the Property Tax Commission
90-PTC-426

---

* * *

QUESTIONS PRESENTED

I. DID THE COURT OF APPEALS CORRECTLY DETERMINE THAT THIS CONTINGENT FEE CONTRACT FOR A TAX AUDITOR'S SERVICES VIOLATES PUBLIC POLICY?

II. DID THE COURT OF APPEALS CORRECTLY DETERMINE THAT THE DISCOVERY OF PHILIP MORRIS U.S.A.'S BUSINESS PERSONAL PROPERTY IS VOID?

III. IS A PROPERTY TAX DISCOVERY BASED ON A CONTINGENT FEE AUDIT CONTRACT UNCONSTITUTIONAL UNDER THE UNITED STATES AND NORTH CAROLINA CONSTITUTIONS?

IV. IS A PROPERTY TAX DISCOVERY BASED ON A CONTINGENT FEE AUDIT CONTRACT NULL AND VOID SINCE A NORTH CAROLINA COUNTY AND ITS TAX ASSESSOR HAVE NO AUTHORITY TO ENTER INTO SUCH A CONTRACT, CONDUCT SUCH AN AUDIT AND RENDER A DISCOVERY BASED ON SUCH AN AUDIT?

* * *

III. CONSTITUTIONAL AND GOVERNMENTAL AUTHORITY PRINCIPLES PROVIDE ADDITIONAL GROUNDS TO VOID THE DISCOVERY.

The Agreement and resulting discovery clearly violate public policy. Furthermore, Philip Morris has properly preserved two additional issues, first by raising them before the Property Tax Commission and then by appealing and cross-appealing them to the Court of Appeals: (i) The discovery based on the contingent fee audit is unconstitutional and (ii) the discovery is void as ultra vires the authority of Cabarrus. These issues provide additional grounds to support the decision of the Court of Appeals. App. R. 10(d) and 28(c) permit Philip Morris to raise these issues. The violation of these fundamental principles supports that the discovery is not only void as against public policy, but is void as a matter of law.

A. THE PROPERTY TAX DISCOVERY BASED ON A CONTINGENT FEE AUDIT CONTRACT IS UNCONSTITUTIONAL UNDER THE UNITED STATES AND NORTH CAROLINA CONSTITUTIONS.

ASSIGNMENT AND CROSS ASSIGNMENT OF ERROR NUMBERS 1 2, 3.

(R pp. 276-77)

EXCEPTION NUMBERS 1, 2 and 3.

(R pp. 262-66, 269-72)

TMA's interest in the audit of Philip Morris was to have Cabarrus issue as high a discovery as possible. This bias infected the entire taxation process depriving Philip Morris of its right to due process of law and to the synonymous North Carolina "law of the land." U.S. Const. amend. XIV; N.C. Const. art. I, § 19.

* * * *

Supreme Court, U.S.
FILED
MAY 31 1994
OFFICE OF THE CLERK

(2)

No. 93-1710

In The

Supreme Court of the United States

October Term, 1993

PHILIP MORRIS INCORPORATED
(d/b/a PHILIP MORRIS U.S.A.),

Petitioner,

v.

CABARRUS COUNTY, NORTH CAROLINA,

Respondent.

On Petition For A Writ Of Certiorari To The Supreme Court Of North Carolina

MOTION OF THE INSTITUTE OF PROPERTY TAXATION TO FILE BRIEF AMICUS CURIAE AND BRIEF AMICUS CURIAE IN SUPPORT OF PHILIP MORRIS INCORPORATED'S PETITION FOR WRIT OF CERTIORARI

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22 pp

No. 93-1710

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TO THE HONORABLE SUPREME COURT OF THE UNITED STATES:

The Institute of Property Taxation, by and through its counsel of record, Edward Kliewer, III, of Foster, Lewis, Langley, Gardner & Banack, Incorporated moves the Court for permission to file a brief amicus curiae in the above entitled case. This motion is made upon the following statements.

STATEMENT AS TO CONSENT

Petitioner Philip Morris Incorporated has consented in writing to the filing of the subject amicus brief.

Respondent Cabarrus County, North Carolina has declined in writing to consent to the filing of the subject amicus brief.

STATEMENT OF INTEREST OF THE INSTITUTE OF PROPERTY TAXATION

The Institute of Property Taxation is a not-for-profit corporation organized under the laws of the District of Columbia with offices at Suite 1150, 888 Seventeenth Street, N.W., Washington, D.C. 20006. The Institute is a nationwide organization with approximately twenty-eight hundred members who represent a great many large and small business corporations in the United States and other professional organizations and individuals having an interest in (1) fostering and promoting uniform and equitable administration of property taxes and other state and local taxes (but not income taxes), and (2) minimizing the costs of administration and compliance with state and local taxation laws.

The Institute pursues its goals through the promotion of education and professionalism of its members, the collection and exchange of information and assistance among its members, cooperation with governmental bodies and the International Association of Assessing Officers for the purpose of improving state and local tax

administration throughout North America, and the establishment and promotion of high standards of competence and efficiency in tax management.

To enhance the education and professionalism of its members, the Institute presents week-long schools in real and personal property taxation and sales and use taxes, as well as forums, symposiums and conferences. It administers two professional certification programs – the CMI ("Certified Member of the Institute") for property tax professionals and the CSM ("Certified Sales Tax Member") for sales tax professionals. Institute members who seek to obtain these professional designations are required to meet rigorous educational and experience requirements and successfully pass comprehensive written and oral examinations.[1]

The Institute has a strong interest in the fair administration of state and local taxes and the issue in this case – payment of contingent fees by an assessing entity for property tax assessment services – is one of national significance since every state has a local property tax system in one form or another. Moreover, the principles at issue have the potential to extend to other forms of taxation.

Therefore, the Institute has an interest in assuring that whatever the Court's decisions as to the issue before it they are made with full appreciation of the importance of this issue.

---

[1] Appended hereto is a statement of the Institute's principles, purposes and its code of ethics.

STATEMENT OF PURPOSE AND SCOPE OF AMICUS BRIEF

It is the opinion of the Institute of Property Taxation that the issue before the Court is one of substantial national importance. The Institute believes that it is well situated to comment upon the national significance of the issue. It is therefore the desire of the Institute to as briefly as possible illustrate the importance of this case. It is the additional desire of the Institute to briefly bring to the Court's attention certain additional authorities and argument relevant to the resolution of the case.

Therefore, the Institute of Property Taxation respectfully requests permission of the Court to submit the enclosed brief in the above-entitled case.

Respectfully submitted,

EDWARD KLIEWER, III
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No. 93-1710

In The

Supreme Court of the United States

October Term, 1993

PHILIP MORRIS INCORPORATED
(d/b/a PHILIP MORRIS U.S.A.),

Petitioner,

v.

CABARRUS COUNTY, NORTH CAROLINA,

Respondent.

On Petition For A Writ Of Certiorari
To The Supreme Court Of North Carolina

BRIEF AMICUS CURIAE OF THE INSTITUTE OF PROPERTY TAXATION FILED IN SUPPORT OF PHILIP MORRIS INCORPORATED'S PETITION FOR WRIT OF CERTIORARI

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STATEMENT OF INTEREST OF THE INSTITUTE OF PROPERTY TAXATION

The Institute of Property Taxation is a not-for-profit corporation organized under the laws of the District of Columbia with offices at Suite 1150, 888 Seventeenth Street, N.W., Washington, D.C. 20006. The Institute is a nationwide organization with approximately twenty-eight hundred members who represent a great many large and small business corporations in the United States and other professional organizations and individuals having an interest in (1) fostering and promoting uniform and equitable administration of property taxes and other state and local taxes (but not income taxes), and (2) minimizing the costs of administration and compliance with state and local taxation laws.

The Institute pursues its goals through the promotion of education and professionalism of its members, the collection and exchange of information and assistance among its members, cooperation with governmental bodies and the International Association of Assessing Officers for the purpose of improving state and local tax administration throughout North America, and the establishment and promotion of high standards of competence and efficiency in tax management.

To enhance the education and professionalism of its members, the Institute presents week-long schools in real and personal property taxation and sales and use taxes, as well as forums, symposiums and conferences. It administers two professional certification programs – the CMI ("Certified Member of the Institute") for property

tax professionals and the CSM ("Certified Sales Tax Member") for sales tax professionals. Institute members who seek to obtain these professional designations are required to meet rigorous educational and experience requirements and successfully pass comprehensive written and oral examinations.[1]

The Institute has a strong interest in the fair administration of state and local taxes and the issue in this case – payment of contingent fees by an assessing entity for property tax assessment services – is one of national significance since every state has a local property tax system in one form or another. Moreover, the principles at issue have the potential to extend to other forms of taxation.

Therefore, the Institute has an interest in assuring that whatever the Court's decisions as to the issue before it they are made with full appreciation of the importance of this issue.

STATEMENT AS TO SCOPE OF BRIEF AMICUS CURIAE

The issue before the Court has been thoroughly and ably addressed by Philip Morris Incorporated in its petition for writ of certiorari. It is therefore not the intent of the Institute to discuss applicable case law in detail. Instead, it is the desire of the Institute to as briefly as possible emphasize the importance of this case and to

[1] Appended hereto is a statement of the Institute's principles, purposes and its code of ethics.

also bring to the Court's attention some additional authorities relevant to the case.

SUMMARY OF ARGUMENT

Contingent fee employment by a property tax assessing authority of a private contractor to perform valuation services instrumental to the determination of a tax liability violates the Due Process Clause of the U.S. Constitution. Contingent fee arrangements and the tax assessment process are fundamentally incompatible. That valuation services and contingent fee arrangements are not compatible is well illustrated by the appraisal profession's prohibition of fees that are contingent upon the value concluded and by specific prohibition of such arrangements under the laws of several states.

ARGUMENT

The issue raised by Petitioner Philip Morris Incorporated is of national importance since property taxation occurs at the local level in one form or another in each of the fifty states. Although property taxation exists in each of the states, the systems of administration of the tax vary widely from state to state. However, all property tax schemes have certain elements in common. These common elements include the fact that property taxation involves two fundamental functions: (1) the determination of the tax liability and (2) collection of the tax once it is determined.

Some states permit taxing authorities to employ private parties to collect taxes, particularly delinquent taxes, and to compensate such private collectors on a contingent fee basis. *See, e.g.*, NEB. REV. STAT. §§ 77-377.01 and .02; N.D. CENT. CODE ANN. § 57-22-29; TEX. TAX CODE § 6.30(c) (1994 Supp.). There is no general unfairness involved in the use of contingent fee arrangements in this phase of the property tax process, because this phase merely involves collection of a tax liability that presumably has been lawfully assessed and is due and owing to the taxing authority.

However, the tax assessment function and contingent fee arrangements are fundamentally incompatible. This is true whether the tax assessment in question involves an original determination of a tax liability or whether, as in the case at bar, the assessment involves a redetermination of a tax liability based upon a "tax audit" or "discovery." While the tax collection process is clearly ministerial in nature, the tax assessment process most certainly is not.

Regardless of whether the tax assessment function is characterized as judicial, quasi-judicial, prosecutorial or otherwise, the essential nature of the process is the same. The value of property generally cannot be determined by simple objective compilation and computation but instead requires examination and analysis of a whole host of factors affecting value – age, physical and market conditions, income potential and obsolescence to name just a few. The appraisal of property, therefore, necessarily involves the use of a substantial amount of judgment. When a person exercising such judgment has a personal pecuniary interest in the outcome of the value decision, the process is inherently tainted. As noted by

the Georgia Supreme Court: "Fairness and impartiality are threatened where a private organization has a financial stake in the amount of tax collections as a result of the assessment it recommends." *Sears, Roebuck and Co. v. Parsons, 260 Ga. 824, 401 S.E.2d. 4, 5 (1991).*

In recognition of the sophisticated nature of the appraisal process, the appraisal industry has become one that is heavily regulated both internally, through various accreditation and standards promulgating bodies, and externally, through state licensing requirements. Significantly, the appraisal industry itself considers appraisal fees that are contingent upon value conclusions to be unethical. The Uniform Standards of Professional Appraisal Practice, promulgated by the Appraisal Standards Board of The Appraisal Foundation[2] expressly provides:

> The acceptance of compensation that is contingent upon the reporting of a predetermined value or a direction in value that favors the

---

[2] The Appraisal Standards Board of the Appraisal Foundation develops, publishes, interprets and amends the Uniform Standards of Professional Appraisal Practice (USPAP) on behalf of appraisers and users of appraisal services. The USPAP is widely used by state and federal regulatory agencies and others. The USPAP have also been adopted by major appraisal organizations in North America and have become the generally accepted standards of appraisal practice. The ethics provision of the USPAP became effective December 4, 1989. ***Foreword to APPRAISAL STANDARDS BOARD OF THE APPRAISAL INSTITUTE, UNIFORM STANDARDS OF PROFESSIONAL APPRAISAL PRACTICE (1993 ed.).*** All members of the Institute of Property Taxation agree to abide by the USPAP pursuant to Rule 18 of the Institute's code of ethics. ***See Appendix.***

> cause of the client, *the amount of the value estimate*, the attainment of a stipulated result, or the occurrence of a subsequent event is unethical.[3]

APPRAISAL STANDARDS BOARD OF THE APPRAISAL FOUNDATION, UNIFORM STANDARDS OF PROFESSIONAL APPRAISAL PRACTICE 2 (1993 ed.) (Emphasis Added).

For similar reasons, at least several states bar the use of contingent fees in the tax assessment process. Texas is one such state. Property taxation in Texas is administered by central appraisal districts generally corresponding to the various counties within the state. ***TEX. TAX CODE ANN. §§ 1.01-43.04 (1994 Supp.)***. The chief administrator of a Texas appraisal district is the "chief appraiser." ***Id.*** Chief appraisers are authorized to employ private firms to provide appraisal services but are expressly prohibited from utilizing contingent fees:

> § 25.01(b) The chief appraiser with the approval of the board of directors of the district may contract with a private appraisal firm to perform appraisal services for the district subject to his approval. A contract for private appraisal services is void if the amount of compensation to be paid the private appraisal firm is contingent on the amount of or increase in appraised, assessed or taxable value of property appraised by the appraisal firm.

TEX. TAX CODE § 22.01(b) (1994 Supp.).

---

[3] It is additionally noteworthy that some states, including North Carolina, specifically bar the use of contingent fees for real estate appraisal assignments. *See N.C. GEN. STAT. § 93A-80(a)(3) (Cum. Supp. 1993).*

As the Petitioner has noted, Georgia is another state which has prohibited the use of contingent fee arrangements, in this instance by decision of the supreme court of the state. *Sears, Roebuck and Co. v. Parsons, 260 Ga. 824, 401 S.E.2d 4 (1991).*

The property tax schemes throughout the country are varied and multitudinous. Similarly, the number of different forms which contingent contracts of the type in question might take are beyond calculation. In the instant case, there are certain circumstances involving both the tax scheme and the particular contract in question which make the additional tax imposed upon Petitioner especially offensive. Chief among these circumstances are:

> (1) once the notice of proposed adjustment was issued the private firm was entitled to significant compensation whether or not the additional tax was ultimately upheld. The taxing authority therefore had an incentive to uphold the tax assessment in order to have funds to pay the private firm;
>
> (2) the private firm apparently had discretion in the selection of the subjects of its audit, discretion which one could reasonably expect to be exercised in a fashion that would likely generate the largest fees (i.e., inequitable targeting of large taxpayers); and
>
> (3) under North Carolina law, tax assessments bear a presumption of correctness. Even erroneous valuations will be upheld unless (a) they are either "illegal" or "arbitrary" and (b) the error is substantial. *See, e.g., Appeal of Amp Incorporated, 287 N.C. 547, 562-63, 215 S.E.2d 752, 761-62 (1975),* and cases cited therein.

Although the particular circumstances of this case make the contingent fee arrangement in question especially offensive, it is the earnest opinion of the Institute that contingent fees are inherently so incompatible with the appraisal/assessment process as to violate due process, regardless of the particularities of the taxation system or contingent fee contract in question.

Taxation is one of the heaviest burdens a government by necessity imposes upon its citizenry. It is therefore of the utmost importance that such burden be administered fairly and objectively. Such fairness and objectivity can never be achieved when a party that is instrumental to the determination of a tax liability has a pecuniary interest in such determination.

CONCLUSION

For all the foregoing reasons, Amicus Curiae the Institute of Property Taxation wholeheartedly endorses the position and arguments of Petitioner and urges that its petition for writ of certiorari be granted.

Respectfully submitted,

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Counsel for Amicus Curiae
Institute of Property Taxation

APPENDIX

THE INSTITUTE OF PROPERTY TAXATION – STATEMENT OF PRINCIPLES, PURPOSES AND CODE OF ETHICS

The Institute of Property Taxation is a non-profit nationwide organization which exists to promote ethical and professional standards of conduct among its members and to administer formal educational programs related to state and local ad valorem, sales and use taxes.

The Institute has a written code of ethics and standards of professional practice, whereby each member agrees to be governed by objective and professional standards consistent with sound administration of property and state and local tax laws and the adoption of tax legislation, with due regard for the interests of society as well as those of the member company. The following are the Institute's Statements of Principles and Purposes and the Code of Ethics.

PRINCIPLES

The Institute of Property Taxation is dedicated to fostering the professionalization of its members, to promoting the uniform and equitable administration of ad valorem taxation and all other forms of state and local taxation (other than income taxation) and to minimizing the costs of administration and compliance.

PURPOSES

In furtherance of the above principles, the Institute of Property Taxation is formed for the following purposes:

1. To foster the education and professionalization of its members and to provide its membership with the information and services necessary to effectively carry out their responsibilities in ad valorem and all other forms of state and local taxation (other than income taxation).

2. To preserve and promote the use of equitable and non-discriminatory methods in taxation of business enterprises carrying on diversified activities in taxing jurisdictions.

3. To eliminate inequitable and discriminatory distortion or otherwise illegitimate methods of determining tax liabilities.

4. To collect, analyze and disseminate information with respect to existing and proposed legislation, regulations and administrative action which is pertinent to the purposes of the Institute; encourage the free discussion of such subjects; present the views of the Institute to other taxpayer organizations, governmental bodies and other interested persons; and take such other actions as are deemed appropriate to the accomplishment of its purposes.

5. To develop and operate a program for the education of its members and to promote the study of property taxation and other forms of state and local taxation (other than income taxation) by encouraging research and by conducting conferences and symposiums on tax matters.

These principles and purposes of the Institute of Property Taxation can be achieved only by the observance of the highest standards of ethical and professional conduct by its members. To insure the observance of these

high standards, the Board of Governors has adopted the following code of ethics.

CODE OF ETHICS
STANDARDS OF PROFESSIONAL CONDUCT

The Institute of Property Taxation has established this Code of Ethics and Standards of Professional Conduct to set forth ethical and professional guidelines for all IPT members in the administration of property and sales and use taxes.

Each member of IPT agrees to subscribe to this Code of Ethics and Standards of Professional Conduct and to report to the IPT Committee on Professional Ethics any unethical practices or actions by any IPT member.

1. IT IS UNETHICAL to engage in any conduct that discredits IPT, or the tax profession.

2. IT IS UNETHICAL to engage in any activity that results in a conviction of any crime that involves the tax profession.

3. IT IS UNETHICAL to operate beyond the boundaries of an agreed relationship with an employer or a client.

4. IT IS UNETHICAL to infer or imply that you represent a person or firm you do not represent, or to file any document on behalf of a taxpayer without specific authorization of the taxpayer.

5. IT IS UNETHICAL to violate the confidential nature of the employee-employer or the consultant-client relationship, except as required by law.

6. IT IS UNETHICAL to offer or accept anything of value with the intent of inducing a specific action.

7. IT IS UNETHICAL to offer or accept anything of value as a share of a fee for an assignment in which you did not participate.

8. IT IS UNETHICAL to assign, accept or perform a tax assignment that is contingent upon producing a predetermined analysis or conclusion.

9. IT IS UNETHICAL to file or proceed with any appeal in which there is known to be no basis in fact. The determination of whether a basis in fact exists must be made as soon as reasonably possible.

10. IT IS UNETHICAL in the performance of a tax assignment to issue an appraisal, analysis or opinion that fails to disclose bias or the accommodation of a personal interest.

11. IT IS UNETHICAL in the performance of a tax assignment to willfully furnish inaccurate, deceitful, or misleading information, or to willfully conceal material information.

12. IT IS UNETHICAL to prepare or use in any manner a resume or statement of professional qualifications that is misleading or false.

13. IT IS UNETHICAL in promoting a tax practice and soliciting assignments to utilize misleading or false advertising.

14. IT IS UNETHICAL in promoting a tax practice and soliciting assignments to make a direct reference to superiority over an individual competitor.

15. IT IS UNETHICAL to solicit any tax assignment by assuring a specific result or by stating a conclusion regarding that assignment without prior analysis of the facts and circumstances pertaining thereto.

16. IT IS UNETHICAL to use client listings or references without specific authorization.

17. IT IS UNETHICAL to make any solicitation implying IPT authorization, endorsement or approval of any product or service.

18. IT IS UNETHICAL in the performance of an independent fee appraisal to violate any part of the "Uniform Standards of Professional Appraisal Practice" issued by The Appraisal Foundation.

Adopted by Board of Governors, April 28, 1991.

MOTION FILED
MAY 27 1994

(3)

No. 93-1710

IN THE
Supreme Court of the United States
OCTOBER TERM, 1993

PHILIP MORRIS INCORPORATED
(d/b/a PHILIP MORRIS U.S.A.),
Petitioner,

v.

CABARRUS COUNTY, NORTH CAROLINA,
Respondent.

On Petition for a Writ of Certiorari to the Supreme Court of North Carolina

MOTION FOR LEAVE TO FILE BRIEF *AMICUS CURIAE* AND BRIEF OF COMMITTEE ON STATE TAXATION AS *AMICUS CURIAE* IN SUPPORT OF PETITIONER

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Counsel of Record
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ELIZABETH C. BURTON
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IN THE

Supreme Court of the United States

OCTOBER TERM, 1993

No. 93-1710

PHILIP MORRIS INCORPORATED
(d/b/a PHILIP MORRIS U.S.A.),
Petitioner,

v.

CABARRUS COUNTY, NORTH CAROLINA,
Respondent.

On Petition for a Writ of Certiorari to the Supreme Court of North Carolina

---

MOTION FOR LEAVE TO FILE BRIEF *AMICUS CURIAE*

The Committee on State Taxation ("COST") hereby respectfully requests leave to file a Brief as *Amicus Curiae* in Support of Petitioner. The interest of COST as *amicus curiae* is described *infra* at Brief, p. 1. Despite COST's qualifications to submit an *amicus* brief, Counsel for Respondent has refused to grant permission to file such a brief, citing inability to meet with his client prior to June 6 (several days after the deadline for filing this brief) to secure a decision in this regard. However, in the absence of such permission there are at least two reasons why this motion should be granted.

First, with respect to the Petition filed in this case, COST has additional observations to make concerning the Due Process implications of the property tax audit scheme being challenged herein. A full exposition of the

controversy and the potential ramifications of this case by each interested and eligible *amicus* is ultimately to the benefit of the Court in its administration of certiorari writs.

Second, in this regard, Philip Morris Incorporated is but one of many members of COST that face audits nationwide by local taxing jurisdictions which utilize independent contract auditors compensated on a contingent fee basis. COST has monitored the development of this practice for several years and is uniquely qualified to comment on the broader concerns and potential consequences of such a practice.

Respectfully submitted,

KENDALL L. HOUGHTON
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WILLIAM D. PELTZ
ELIZABETH C. BURTON
Chair and Vice Chair, Lawyers' Coordinating Subcommittee
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Dated May 27, 1994

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1993

No. 93-1710

PHILIP MORRIS INCORPORATED
(d/b/a PHILIP MORRIS U.S.A.),
Petitioner,

v.

CABARRUS COUNTY, NORTH CAROLINA,
Respondent.

On Petition for a Writ of Certiorari to the Supreme Court of North Carolina

BRIEF OF COMMITTEE ON STATE TAXATION AS *AMICUS CURIAE* IN SUPPORT OF PETITIONER

INTRODUCTORY STATEMENT

This brief is submitted by the Committee on State Taxation as *amicus curiae* in support of Petitioner in the above-captioned matter. Written consent of the Petitioner has been obtained and filed with the Clerk of the Court; the Motion for Leave to File a Brief *Amicus Curiae* is made because the Respondent has refused to likewise grant permission to file a brief.

INTEREST OF *AMICUS CURIAE*

The Committee on State Taxation ("COST") is a non-profit trade association that was organized in 1969 as an advisory committee to the Council of State Chambers of Commerce. COST, which was separately incorporated on

January 1, 1992, has a membership of over 420 major multistate corporations, engaged in interstate and international business. COST's objective is to preserve and promote equitable and nondiscriminatory state and local taxation of multijurisdictional entities.

Many of COST's members are engaged in business in states where local taxing jurisdictions have employed independent contractors to perform their administrative and audit functions relating to property taxes, sales and use taxes, and other taxes imposed at the local level of government. While the behavior of Cabarrus County, North Carolina lies at one end of the continuum of involvement of outsiders in the local tax administration process, as discussed in this Brief, the number of variations on the theme of utilization of independent contingent fee auditors is surprising and confusing. COST's member corporations are often the largest taxpayers in a local jurisdiction, and bear the greatest brunt of any unconstitutional or unequitable taxing scheme implemented by that jurisdiction. COST is concerned with the Due Process implications of such practices, wherever they may occur, and hence has an interest in this case.

SUMMARY OF ARGUMENT

A broad range of relationships can be structured between local governments and independent third parties, in order to facilitate the government's completion of its tax administrative and audit functions. Certainly, some arrangements will imbue the independent contractors with greater agency powers than others; but in every case, the relationship is circumscribed by the basic Due Process requirements that the governing body engage in "fair play" with, and provide "substantial justice" to, its taxpayers. In this case, the relationship violates Due Process principles in at least two respects:

(i) the contract auditors are permitted to choose their own audit targets, rather than being assigned random targets;

(ii) contingent fees are utilized to compensate contract auditors whose proposals are issued as "discoveries" to taxpayers; and

(iii) these discoveries, rather than the tax liability ultimately collected, are the measure of the fee owed them by Cabarrus County, thus resulting in the creation of a financial interest on the part of the County in the preservation of a sufficient tax liability to at least cover the contingent fee.

Contrasting Cabarrus County's practice to the approved practice of paying contingent fees to informants who assist law enforcement officials in state prosecutions illustrates the constitutional infirmities of the practice at issue in this case. First, a compelling interest in preserving the integrity of the law enforcement system justifies the use of contingent fees to compensate informers. Second, where a contingent fee informant's testimony is used in a state prosecution, ample Due Process protections are afforded to the defendant, including: (i) the use of a jury, (ii) full submission to the jury of the question of credibility of such a witness (through cross examination of the witness, notification of the contingent fee arrangement, and instructions to the jury), and (iii) submission of other corroborating testimony at trial. None of these specific Due Process protections are afforded a Cabarrus County taxpayer who is audited by a contingent fee contract auditor, nor may the structural bias against the taxpayer be countered in any other way by first level review of a proposed assessment of Cabarrus County property taxes.

The variety of theories put forth by the State courts, both in support and condemnation of the practice of paying contract auditors contingent fees, illustrates the need for a clear resolution by this Court of the Due Process principles applicable in this arena.

ARGUMENT

I. ON THE SPECTRUM OF LOCAL JURISDICTION PRACTICES OF UTILIZING INDEPENDENT AGENTS TO PERFORM TAX ADMINISTRATIVE AND AUDIT FUNCTIONS, THE COMPENSATION OF SUCH AGENTS BY CONTINGENT FEES CLEARLY VIOLATES DUE PROCESS

There is a broad spectrum of relationships which may be structured between counties, municipalities, or other local governments and independent third parties, for purposes of accomplishing local tax administrative functions. Some of the relationships, as described below, pose no grounds for objection by taxpayers. However, some relationships offend the Due Process Clause tenets of "fair play" and "substantial justice," applicable to the taxpayers of both State and local jurisdictions. *International Shoe Co. v. Washington*, 326 U.S. 310 (1945).

The spectrum of relationships between local jurisdictions and independent agents which COST has identified, based upon a study of case law and current local practices reported to it by its members, is presented below in order from the clearly constitutional (at least on its face) to the clearly unconstitutional schemes:

1. Pure Governmental Administration/Auditing (No Relationship with Independent Agents):

This practice is obviously the norm for state and local tax administration and auditing of taxpayers. However, while state departments of revenue generally have sufficient staff to perform all such functions, local jurisdictions with responsibility for tax collections and audits may be less well-staffed and hence resort to outside assistance. The various manners in which such contract auditors are employed and compensated are discussed below.

2. Contract Auditor Examines Only Materials Filed with Local Jurisdiction/No Contingent Fees:

In this case, a limited agency has been established. For instance, a local jurisdiction might employ contract as-

sistants "not to do audits, but rather to compare details written into the different governmental required reports." *Union Pacific Resources Co. v. State*, 839 P.2d 356, 374 (Wyo. 1992). To the extent such limited, essentially non-audit, activity is not compensated on a contingent fee basis, no Due Process question arises.[1]

3. Contract Auditor Examines Internal Records of Taxpayer/No Contingent Fees:

This arrangement extends the authority of the contract auditor, to directly contact a taxpayer and audit its books and records. In *General Motors Corporation v. State Tax Commission*, 200 Mich. App. 117, 504 N.W.2d 10 (1993), *appeal dismissed*, 509 N.W.2d 157 (Mich. 1993), the City of Warren hired an outside accounting firm to conduct an audit of General Motors, a taxpayer believed by the City to have underreported its taxable personal property. The Court of Appeals of Michigan held that state statutory authority existed for "[t]he commission or any duly authorized representative thereof" to examine the property, books and records of any person owning property liable to assessment for taxes, and properly distinguished the *Sears, Roebuck & Co. v. Parsons*, 260 Ga. 825, 401 S.E.2d 4 (1991), and *Philip Morris* (Court of Appeals) decisions:

> Unlike those cases, the present case does not involve a contingent fee arrangement, nor is [the contract auditor] afforded the discretion to choose the target of the audit.

General Motors, 504 N.W.2d at 12.

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[1] In fact, the above-cited *Union Pacific Resources* case did involve contingent fees and thus belongs further down the spectrum toward the point where this case lies.

4. Contract Auditor Picks (Or Is Assigned [2]) Audit Target/Is Paid a Contingent Fee—

(i) based on tax liabilities ultimately collected; or

(ii) based on what is "discovered" or proposed as a liability by contract auditor:

These are the most egregious arrangements between local jurisdictions and contract auditors. The taxing authority essentially "leverages" jurisdictional tax revenues by paying contract auditors with the very funds raised by them through audit assessments. In the first instance above, the leveraging is less direct although still oppressive. However, the offense to Due Process in the second instance, which in fact is the scheme at issue in this case, is patent. The agent's financial interest, and hence the local government's financial interest, in the outcome of the proceedings is established from the moment the contract auditor's proposals are issued as a "discovery." The "discovery" of taxable property or undervaluation of same is the event triggering the liability of the County to the contract auditor, in the amount of 35% of that discovered amount, regardless of subsequent reductions in the tax liability proposed, due as a result either of informal conferences/settlements or of formal appeals. The resultant structural bias to find sufficient tax due to at least cover the contingent fee precludes a fair and impartial assessment of any taxpayer so identified and audited.

Nevertheless, the Supreme Court of North Carolina barely gave lip service to the constitutional principles in-

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[2] As noted in the Petition, p. 4, permitting the contract auditors to identify their audit targets is at least likely, if not guaranteed, to result in a less than "random" sampling of taxpayers within the jurisdiction, particularly if the auditors are not subject to a limit on the contingent fees they can earn. Likewise, these "deep pocket" audit targets are very likely to be subjected to more aggressive and less impartial audits. However, both practices are included together for the sake of brevity, and because the more extreme practice is the one at issue in this case.

volved in this case; and other State courts have come out with conflicting positions on this question. The Georgia Supreme Court recognized the public policy and Due Process issues at stake and stated in *Sears, Roebuck & Co. v. Parsons,* 401 S.E.2d at 5: "The people's entitlement to fair and impartial tax assessment lies at the heart of our system, and, indeed, was a basic principle upon which this country was founded." *But see Dillon Stores v. Lovelady,* 253 Kan. 274, 855 P.2d 487, 491 (1993). In *Dillon Stores,* contingent fee contracts were held not to violate Kansas public policy. There, the contract auditors chose audit targets and were compensated on an hourly rate basis with a maximum 35% contingent fee keyed to additional taxes assessed by the county. (This form of compensation is essentially an hourly rate, *limited* by a measure of the tax found.)

If this Court believes that the concerns over systemic fairness and undue deprivations of property that underlie the Due Process Clause are wrongly disregarded by Cabarrus County and other local jurisdictions that utilize contingent fee compensation arrangements, then it should clarify this fact for taxpayers and State and local governments alike.

II. A COMPARISON OF THE USE OF CONTINGENT FEES TO COMPENSATE INFORMANTS IN STATE CRIMINAL PROSECUTIONS ILLUSTRATES THE IMPROPRIETY OF USING SUCH A COMPENSATION SCHEME WITH RESPECT TO STATE TAX ADMINISTRATIVE AND AUDIT FUNCTIONS

The constitutional infirmities of contingent fee compensation of contract auditors become manifest when that practice is contrasted with the generally approved practice of compensating informants in state prosecutions by means of contingent fees.

It has long been the practice of state and local law enforcement agencies to utilize contingent fee arrangements to secure the assistance of informers in identifying,

arresting and prosecuting individuals involved in criminal activity. Challenges to this version of the "bounty hunter" practice have been made on both public policy and due process grounds, but rarely have such challenges been successful. Courts that have analyzed the propriety of contingent fee arrangements with informants have affirmed the necessity of such arrangements to effective law enforcement, as a matter of public policy. *See, e.g., Williams v. State,* 463 So.2d 1064 (Miss. 1985); *State v. Maddasion,* 130 Ariz. 306, 636 P.2d 84 (1981); *People v. Mills,* 40 Ill.2d 4, 237 N.E.2d 697 (1968) (noting additionally that the type of individual who can assist law enforcement officials in criminal cases generally has not led a blameless life and must be enticed into giving such assistance). Thus, a compelling interest exists in this context to justify the use of contingent fee compensation. Of course, concomitant with this conclusion, such courts note the procedural Due Process protections that are afforded defendants in cases where contingent fee informant testimony is utilized, including: (i) the use of a jury, (ii) full submission to the jury of the question of credibility of a contingent fee witness (through notification of the contingent fee arrangement, cross examination of the witness, and detailed jury instructions), and (iii) submission of other corroborating testimony at trial. *See* 57 A.L.R. 4th 643, sec. 12[c] (citations omitted).[3]

Even in the context of state prosecutions, the use of contingent fees has been disapproved by courts as violative of Due Process if the "ever present danger of governmentally subsidized perjury," *see United States v. Ladley,*

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[3] A similar scheme has been instituted by the Internal Revenue Service. The IRS Informant Program is embodied in I.R.C. § 7623, which contains the terms for rewarding individuals who provide information on possible noncompliance with federal tax laws. Like the state informants program, and *unlike* the Cabarrus County contract auditors program, the individual against whom such information is provided faces potential criminal prosecution and is afforded ample Due Process protections.

517 F.2d 1190 (9th Cir. 1975), is realized. For instance, in *State v. Glosson,* 441 So.2d 1178 (Fla. App. 1st Dist. 1983), *aff'd.*, 462 So.2d 1082 (Fla. 1985), the informant was paid a contingent fee upon successfully making criminal cases against others to whom he sold controlled substances supplied by the local sheriff's department; and in this case, the contingent fee testimony constituted the entire case against the defendant. The Supreme Court of Florida prohibited the creation of such a direct financial stake in criminal convictions, on grounds that there were few situations imaginable with more potential for abuse of a defendant's Due Process rights.

The practice of compensating informants in state prosecutions has generally been deemed constitutional, because defendants' Due Process rights are afforded protections that counterbalance the potential bias to them. By contrast, the practice adopted by Cabarrus County in this case of compensating contract auditors on a contingent fee basis is clearly violative of taxpayers' Due Process rights.[4]

First, there is no compelling interest on the part of local jurisdictions in enforcement of state tax laws that justifies the use of contingent fee auditors. The tax system in this country has been structured as an "honor system" based upon self-assessment, and the instances of egregious taxpayer behavior do not justify "bounty hunting" of taxpayers who are remiss in their tax compliance. Rather, as most of the state jurisprudence in this area recognizes (and as the lower courts in North Carolina concluded in this case), Due Process mandates the fair and impartial assessment of all taxpayers—a mandate

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[4] In fact, the Cabarrus County practice is fraught with even more potential for abuse than the practice condemned in *State v. Glosson, supra.* Here, the contingent fee award is paid on the mere accusation (accusation being the "discovery" of taxable or undervalued property that results in the mailing of a notice of proposed additional tax liability), versus a successful prosecution.

that is inconsistent with creation of a financial stake in the outcome of audits on the part of auditors. *See Sears, Roebuck, supra.*

Second, in the context of this case, there are *no* significant procedural Due Process safeguards available to County taxpayers who are subject to a "discovery" of taxable property or undervaluations as the result of a contract auditor's proposals. None of the protections afforded criminal defendants subject to contingent fee witness testimony are available to the Cabarrus County taxpayer who is audited by a contingent fee contract auditor. As noted in the Petition, pp. 17-19, the first level review of a proposed assessment cannot remove the bias against the taxpayer that results from the financial interest in the audit outcome that both the contract auditors and the County hold. Even without addressing the potential abuses of authority that may occur in this context (*e.g.*, intentional overvaluation of reported property, or "discovery" of property that is not in fact taxable), the near impossibility of receiving an adjustment in aggressive proposed assessments made by contingent fee auditors, who will in any event be entitled to payment by the County of a percentage of such amounts discovered by them, renders such a practice in the arena of state and local taxation void under the Due Process Clause.

CONCLUSION

For the reasons set forth above, the Committee on State Taxation respectfully requests that the Court grant a writ of certiorari in this case.

Respectfully submitted,

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Dated May 27, 1994

MOTION FILED
MAY 31 1994

No. 93-1710

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CABARRUS COUNTY, NORTH CAROLINA,
Respondent.

On Petition for a Writ of Certiorari to the Supreme Court of North Carolina

MOTION FOR LEAVE TO FILE BRIEF *AMICUS CURIAE* IN SUPPORT OF PETITIONER AND BRIEF *AMICUS CURIAE* FOR NORTH CAROLINA CITIZENS FOR BUSINESS AND INDUSTRY

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PRESS OF BYRON S. ADAMS, WASHINGTON, D.C. 1-800-347-8208

16 pp

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Respondent.

On Petition for a Writ of Certiorari to the Supreme Court of North Carolina

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MOTION FOR LEAVE TO FILE BRIEF *AMICUS CURIAE* IN SUPPORT OF PETITIONER

North Carolina Citizens for Business and Industry hereby respectfully moves for leave to file the attached brief *amicus curiae* in this case. The consent of the attorney for the petitioner has been obtained. The consent of the attorney for the respondent was requested but refused.

North Carolina Citizens for Business and Industry ("NCCBI") was founded in 1942 as a non-profit, non-

partisan organization dedicated to the creation of a better business environment in North Carolina. NCCBI, whose members include over 1,500 companies representing every sector of the North Carolina business community, is recognized as a leading advocate of industry's position on issues affecting North Carolina business.

The decision of the North Carolina Supreme Court in this case sanctioning the use by counties of contingent fee auditors affects the rights of members of NCCBI and all other North Carolina taxpayers to fair and impartial property tax assessments.

NCCBI, through its members, has a broader perspective on the practices of contingent fee auditors in North Carolina than does the petitioner. Members of NCCBI have been audited by counties other than Cabarrus County and by contingent fee auditors other than the auditors which audited the petitioner. Also, members of NCCBI own a wider range of business property than does the petitioner, and thus the membership of NCCBI has experienced due process violations not experienced by petitioner.

Members of NCCBI have also had broader experiences with the county assessors with whom contingent fee auditors work and with the county boards which review the assessments derived from the work of contingent fee auditors.

The broad experience of NCCBI members with contingent fee auditors and the process of property tax assessment in North Carolina in general renders NCCBI uniquely capable of assisting the Court in understanding the ways in which the use of contingent

fee auditors have violated the due process rights of North Carolina taxpayers.

Respectfully submitted,

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BRIEF OF NORTH CAROLINA CITIZENS FOR BUSINESS AND INDUSTRY AS *AMICUS CURIAE* IN SUPPORT OF PETITIONER

INTRODUCTORY STATEMENT

This brief is submitted by North Carolina Citizens for Business and Industry as *amicus curiae* in support of petitioner in the above-captioned case. Written consent of petitioner has been obtained and has been filed with this Court. The consent of respondent was requested but refused.

INTEREST OF *AMICUS CURIAE*

North Carolina Citizens for Business and Industry ("NCCBI") was founded in 1942 as a non-profit, non-partisan organization dedicated to the creation of a better business environment in North Carolina. NCCBI, whose members include over 1,500 companies representing every sector of the North Carolina business community, is recognized as a leading advocate of industry's position on issues affecting North Carolina business.

The decision of the North Carolina Supreme Court in this case sanctioning the use by counties of contingent fee auditors affects the rights of members of NCCBI and all other North Carolina taxpayers to fair and impartial property tax assessments.

SUMMARY OF ARGUMENT

Contingent fee audit contracts used to assist in the property tax process violate the Due Process Clause of the Fourteenth Amendment because they provide an incentive to produce unfairly high tax assessments. The role of the contingent fee auditor involves the exercise of significant judgment and discretion which directly affects the final assessments issued by county assessors. The interest of the contingent fee auditor in the highest possible assessment so permeates the assessment process as to irremediably taint the assessment. This problem has been exacerbated by the fact that the work of contingent fee auditors in North Carolina has been inadequately supervised because most tax assessors have inadequate training, expertise and experience to be able to properly oversee the activities of these auditors, particularly in the complex area of personal property assessment.

The review procedure provided by North Carolina law is inadequate to remedy the due process violations inherent in contingent fee audits. Not only does the taxpayer have the burden of proof to prove that the assessment derived from the contingent fee audit was arbitrary or illegal and that the assessment substantially exceeded the true value in money of the property assessed, the taxpayer must prove this before a county board which itself has an interest in the highest possible assessment and which is highly deferential to the actions of the county assessor.

ARGUMENT

I. THE USE OF CONTINGENT FEE AUDITORS IN MAKING PROPERTY TAX ASSESSMENTS VIOLATES THE DUE PROCESS CLAUSE.

A contract that gives a person engaged in determining tax liability a direct financial interest in the amount of taxes assessed gives that person an incentive to induce the local government to issue as high an assessment as possible. The bias inherent in such a contract necessarily infects the entire assessment process and deprives taxpayers of an impartial adjudicator in violation of the Fourteenth Amendment to the United States Constitution, which prohibits the states from depriving any person of property without due process of law.

This Court held in *Tumey v. Ohio*, 273 U.S. 510 (1927), that the Due Process Clause requires that a judicial officer have no pecuniary interest in the outcome of an adjudication. *Tumey* involved a mayor acting as judge in a proceeding from which he received a percentage of the fine he imposed. This Court

stated: "That officers acting in a judicial or quasi-judicial capacity are disqualified by their interest in the controversy to be decided is, of course, the general rule." 273 U.S. at 522.

In tracing the right to a judicial officer free of pecuniary interest back to the Middle Ages, the Court stated flatly that, "the slightest pecuniary interest of any officer, judicial or quasi-judicial, in the resolving of the subject matter which he was to decide, rendered the decision voidable." 273 U.S. at 524.

The general rule is that the assessment process is a judicial or quasi-judicial process. In *Hagar v. Reclamation District No. 108*, 111 U.S. 701 (1884), this Court stated: "where a tax is levied on property not specifically, but according to its value, to be ascertained by assessors appointed for that purpose upon such evidence as they may obtain, a different principle comes in. The officers in estimating the value act judicially." 111 U.S. at 710.

The Court added that, "the duties of assessors in estimating the value of property for purposes of general taxation are judicial." 111 U.S. at 710 n.

In the instant case, the auditing work performed by the contingent fee auditor was an integral part of the assessment function. The activities of the auditor were completely interwoven with the activities of the assessor. The assessment itself was the direct result of the work of an auditor with a pecuniary interest in a high assessment. (Petitioner's Appendix 26a.)

In an *amici curiae* brief in support of the use of contingent fee auditors which was filed by the North Carolina Association of County Commissioners and North Carolina League of Municipalities with the

Supreme Court of North Carolina in this case, the *amici curiae* pointed out that approximately 27 of the 100 counties in North Carolina have used contingent fee auditors for the property tax assessment of business personal property. Thus, the use of contingent fee auditors is a pervasive practice in North Carolina.

The *amici curiae* also pointed out that with few exceptions, North Carolina counties do not employ auditors on their assessors' staffs. This lack of in-house expertise inevitably renders it difficult, if not impossible, for an assessor to effectively supervise the contingent fee auditor or evaluate the auditor's report.

It has been the experience of NCCBI members that North Carolina assessors have generally accepted, without significant change, the recommendations of contingent fee auditors, in effect merely rubber stamping their reports, which then become the assessments. Thus, the auditor, with a pecuniary interest in the highest possible assessment, is the true decision maker in most contingent fee audits in North Carolina.

Personal property tax auditing is a complex process encompassing the review of a broad range of taxpayer records and requiring the exercise of the auditor's judgment throughout the process. This exercise of discretion in large part determines the value conclusions inherent in an assessment. Contingent fee auditors auditing members of NCCBI have made decisions such as those listed below:

(a) selective decisions as to what taxpayer records to review or to exclude from review or consideration;

(b) the classification of particular items of property as real property or personal property or mixed real property and personal property. As an example, boilers for heating systems, air conditioning, wiring, venting, flooring, conveyors, shelving and displays are all items that may be considered either real estate or personalty and as such subject to different valuation techniques;

(c) the classification and valuation of items of inventory as raw inventory, work in process, or finished product;

(d) in the event that certain cost data and dates of acquisition are unavailable, the estimation of the value of particular items of personalty;

(e) the determination of whether entries on a taxpayer's books reflect property which is properly assessable;

(f) the classification of particular items of machinery and equipment into categories which have short lives and rapid depreciation resulting in lower assessments or into categories with longer lives and less rapid depreciation resulting in higher assessments;

(g) the recommendation of trending and depreciation tables used by counties to value machinery and equipment, the decision as to which may result in higher values or lower values depending upon which tables are recommended by the auditor and accepted by the assessor.

Further, in many counties, contingent fee auditors have been given broad discretion as to choice of audit

targets, invariably choosing the larger taxpayers in the county for audit.

In short, in the instant case and in other cases in which contingent fee auditors have audited members of NCCBI, the role of the contingent fee auditor has involved significant judgment and discretion, particularly given the typical assessor's lack of resources and independent expertise. An inevitable bias towards inflated assessments is inherent in this process.

II. THE COUNTY REVIEW PROCEDURE DOES NOT CURE THE DUE PROCESS VIOLATION.

The procedure required by North Carolina law and followed by North Carolina counties in reviewing a decision of an assessor is not adequate to remove the taint of the pecuniary interest of the contingent fee auditor from the assessment rendered by the assessor acting on the contingent fee auditor's recommendation.

In North Carolina, tax assessments rendered by an assessor are presumed to be correct and the burden of proof is on the taxpayer to show that the assessment is erroneous. In order to rebut the presumption of correctness, the taxpayer must produce competent, material and substantial evidence that the assessor used an arbitrary or illegal method of valuation *and* that the assessment substantially exceeded the true value in money of the property. *Appeal of McElwee, et. al*, 304 N.C. 68, 75, 283 S.E.2d 115, 120 (1981); *Appeal of AMP, Inc.*, 287 N.C. 547, 562-63, 215 S.E.2d 752, 761-62 (1975). While this burden of proof may be appropriate where the assessment is made by one with no financial interest in the outcome, it is constitutionally offensive where the assessment process

is tainted by the use of a contingent fee auditor who has a direct financial interest in the assessment. In this latter situation, the underlying basis for presuming the correctness of a tax assessment does not exist.

Under North Carolina law, an assessor's decisions are subject to review by the county commission, the elected governing body of each county, sitting as the board of equalization and review or by a special board of equalization and review appointed by the county commissioners. N.C. Gen. Stat. § 105-312 and N.C. Gen. Stat. § 105-322. If the commissioners decide to appoint a special board of equalization and review, the special board often includes members of the county commission themselves and it generally meets for only a limited period of time. At all other times, appeals from assessments are heard by the county commission.

The assessor is a county employee appointed by the board of county commissioners. N.C. Gen. Stat. § 105-294(a). The board inevitably relies on the supposed expertise of the assessor and is not likely to overturn his decision. More frequently than not, if any action is taken other than approving the assessment, in complex cases the board will merely remand the assessor's decision to the assessor for further consideration rather than attempt to resolve the case itself.

County commissioners in North Carolina are under great pressure to raise revenues in order to meet the increasing demands placed upon county governments for social services and other spending. Unfunded mandates imposed upon counties by state government also exert pressure on county commissioners to raise revenues. County commissioners are under significant political pressure to keep taxes on homeowners low. All

of these factors frequently result in the overly aggressive—and unfair—pursuit of business taxpayers.

A business taxpayer, when confronted with the necessity to appeal an inflated assessment made by an assessor based upon the recommendation of a contingent fee auditor, finds itself facing not only the burden of proof to prove that the assessment is wrong and substantially excessive, but having to meet this heavy burden before a body predisposed to approve the assessment without change in order to increase revenues in the least politically painful fashion.

The same concerns for due process that impelled the decision of this Court in *Tumey v. Ohio*, *supra*, and *Ward v. Village of Monroeville*, 409 U.S. 57 (1972), are present in this case. County commissioners, even though they do not profit personally from ad valorem tax assessments, have such a stake in the outcome of the proceedings in which a taxpayer challenges an assessment produced by a contingent fee audit that the review process cannot remove the taint of the contingent fee audit which resulted in the challenged assessment.

The experience of NCCBI members has been that the county appeals process does not remove the taint of an unfair assessment. If anything, the local appeals process exacerbates the due process violations inherent in the contingent fee audit process, given the burden of proof placed upon a taxpayer to rebut a tainted assessment not rendered by a disinterested assessor and the pressures on county commissioners to produce a balanced budget.

CONCLUSION

For all of the foregoing reasons, North Carolina Citizens for Business and Industry respectfully request that petitioner's Petition for Writ of Certiorari be granted.

Respectfully submitted,

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Dated: May 31, 1994

Supreme Court, U.S.
FILED
MAY 27 1994
OFFICE OF THE CLERK

No. 93-1710

In The

Supreme Court of the United States

October Term, 1993

PHILIP MORRIS INCORPORATED
(d/b/a PHILIP MORRIS U.S.A.),

Petitioner,

v.

CABARRUS COUNTY, NORTH CAROLINA,

Respondent.

On Petition For A Writ Of Certiorari To The Supreme Court Of North Carolina

RESPONDENT'S BRIEF IN OPPOSITION

RECEIVED
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QUESTION PRESENTED

Whether a local government may pay for property tax auditing services on a percentage-fee basis without violating the requirements of the Due Process Clause of the Fourteenth Amendment.

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No. 93-1710

In The

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October Term, 1993

PHILIP MORRIS INCORPORATED
(d/b/a PHILIP MORRIS U.S.A.),

Petitioner,

v.

CABARRUS COUNTY, NORTH CAROLINA,

Respondent.

On Petition For A Writ Of Certiorari To The Supreme Court Of North Carolina

RESPONDENT'S BRIEF IN OPPOSITION

Respondent Cabarrus County, North Carolina, respectfully requests that the Court deny the petition for a writ of certiorari seeking review of the opinion of the Supreme Court of North Carolina reported at 335 N.C. 227, 436 S.E.2d 828 (1993).

JURISDICTION

Petitioner has sought review under 28 U.S.C. § 1257. The decision below should not, however, be deemed final within the meaning of this statute. *See infra* pp. 13-14. For

this reason, the case does not lie within this Court's jurisdiction.

STATEMENT OF THE CASE

Cabarrus County is a largely rural county of approximately 100,000 residents in central North Carolina. As its primary source of revenue, the County taxes real and personal property, and requires all taxpayers to list their property as of January 1 each year. For owners of business personal property, such as a cigarette manufacturing facility with extensive machinery and equipment, the County requires that 100 percent of the original historic costs of this equipment be listed, along with the year of acquisition. The County then applies trending tables recommended by the North Carolina Department of Revenue to depreciate these costs. Property tax assessments are made on the basis of these depreciated amounts.

Under North Carolina statutes, each county assessor is required "to see that all property not properly listed during the regular listing period be listed." N.C. Gen. Stat. § 105-312(b). Whenever an assessor finds unlisted or underlisted property, he must issue a discovery assessment. *See id.* § 105-312(d).

Prior to 1988, Cabarrus County did not audit business personal property taxpayers. In response to concerns about possible underlisting of property, the Cabarrus County assessor in early 1988 retained a firm on a percentage-fee basis to conduct tax audits. *See* N.C. Gen. Stat. § 105-296(a). This contract was approved by the Board of County Commissioners. *See id.* § 105-299. A

short time after the auditors were employed, the county assessor (not the auditors) selected the businesses to be audited. The assessor had no financial or personal interest in the outcome of any audit or discovery. An estimated 600 business personal property audits were directed by the county assessor, and in approximately two-thirds of the audits, the taxpayers had reported their costs accurately. Approximately five percent of the taxpayers had over-reported their costs and were informed that they were entitled to refunds. The remainder had under-reported their costs and were sent discovery notices.

In the fall of 1988, the assessor wrote Philip Morris to request that its internal cost and asset records be made available for an audit. Despite several verbal and written requests over a period of nine months, Philip Morris refused to make its records available. The assessor then issued a jeopardy assessment to assure that the statute of limitations would not expire.[1] Philip Morris' attorneys finally sent copies of the needed records in December 1989, over a year after they were requested.

These records revealed that, for each year between 1984 and 1989, Philip Morris had listed less than one-half of the costs for its business personal property located in Cabarrus County, rather than the full actual costs as required. Indeed, before the North Carolina Property Tax Commission, Philip Morris stipulated to cost figures that showed that it had listed less than one-half of its costs. By

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[1] This assessment was for the total value of the property. The actual tax would have been approximately one percent of the assessed amount.

underlisting its business personal property, Philip Morris avoided over one million dollars per year of property taxes in Cabarrus County.[2]

In early 1990, the auditors completed their review of Philip Morris' records and filed a preliminary report of the Philip Morris underlistings to the assessor. The Cabarrus County assessor reviewed this report and then met with Philip Morris officials, attorneys and other representatives on several occasions. The Cabarrus County assessor then made his decision to issue the subject discovery assessment on May 8, 1990. The assessor's discovery assessment was less than the auditor's report, because Philip Morris persuaded the assessor that certain property was exempt from taxation or otherwise should not be included in the discovery.

After an appeal hearing was concluded before the local equalization and review board, the state Property Tax Commission by a 3-2 vote ruled that the discovery was null and void because the auditors' percentage-fee contract violated state public policy. Prior to the ruling, the parties submitted no affidavits and no testimony; the ruling was based on Philip Morris' motion and argument by counsel. The Court of Appeals affirmed without holding oral argument. On December 3, 1993, the Supreme Court of North Carolina reversed the decision of the Court of Appeals, ruling that the auditors' percentage fee contract did not violate public policy and thus the discovery was valid. The Supreme Court remanded the case for

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[2] Philip Morris' financial statements reflect that its operating profit on the cigarettes from the Cabarrus County facility substantially exceeds one *billion* dollars per year.

a hearing on the merits by the Property Tax Commission. Such hearing commenced May 9, 1994, and while the evidentiary hearing has been concluded, a final decision of the Commission has not been rendered as of this date.

Before both the North Carolina Court of Appeals and the Supreme Court of North Carolina, Philip Morris pressed its due process argument that the auditor should be viewed as a judicial official. Philip Morris did not, however, argue that the auditor should be viewed as a prosecutorial official.

SUMMARY OF ARGUMENT

Petitioner, one of the largest and most profitable consumer products companies in the world, seeks to continue avoiding its local tax obligations by asking this Court to decide if due process prevents a local government from hiring a private company as tax auditor and compensating it on a percentage-fee basis. Respondent Cabarrus County used such a system out of necessity because it had no budgeted funds to hire staff auditors. The system has benefitted the County by uncovering underlisting of business personal property that had previously deprived the County of substantial revenue. Such revenue funds county schools, social services, and municipal projects.

There are strong reasons to conclude that this issue does not require the Court's attention, particularly as it is presented in this case. First, the issue is notably uncontroversial. No court has found a due process violation in such circumstances. Indeed, only one other state court

has even addressed this due process issue, and that court, like the court below, found no constitutional violation.

In apparent recognition that the question presented does not involve a conflict or an issue of practical importance, petitioner contends that the issue is one of at least academic interest. This contention is undermined by *Tumey v. Ohio*, 273 U.S. 510, 535 (1927), where this Court recognized that offering rewards to citizens for their aid in the apprehension of wrongdoers raised no due process difficulties. The same rule applies here. The limited function played by the tax auditor in Cabarrus County and the multi-layered review process leave no doubt that the procedures here satisfied the requirements of due process.

Finally, even if there were serious questions as to the constitutionality of the procedures here – a proposition that respondent emphatically rejects – this case would present a particularly inappropriate vehicle for resolving them. The decisions below gave little discussion to the constitutional issue. The issue was presented and decided without any factual record on significant aspects of the auditor's duties, even though there were disputes as to the nature of those duties. The lack of jurisprudential guideposts combined with unresolved factual issues makes this case a poor candidate for review.

Even more important, this case does not appear to satisfy the finality requirement of 28 U.S.C. § 1257. Petitioner is continuing to contest its tax liability on non-constitutional grounds in state proceedings, and the merits of the case have not been resolved. The case does not fall within any established exception to the finality

requirement. Even if this apparent lack of finality did not deprive this Court of jurisdiction, it would argue against use of this Court's limited resources here, since it is possible that further proceedings will moot the issue.

REASONS FOR DENYING THE WRIT

I. THE DECISION BELOW DOES NOT MERIT REVIEW, SINCE IT INVOLVES NEITHER A CONFLICT NOR AN IMPORTANT FEDERAL QUESTION.

The established grounds for discretionary review – a conflict in the case law or a federal question of exceptional importance – are simply not present in this case. *See* Sup. Ct. R. 10.1. Instead of pointing up a sound basis for review, the authority cited by petitioner tends to show that the due process implications of the compensation of tax auditors is an issue involving no controversy. *See* Pet. at 9, 20.

In fact, of the several state cases cited by petitioner, only one case even addressed the argument that due process precluded paying tax auditors on a contingency basis – and that case unceremoniously rejected the argument. *Union Pacific Resources Co. v. State*, 839 P.2d 356, 377 (Wyo. 1992). The other state cases on which petitioner relies did not address constitutional issues, but considered whether various compensation arrangements offended public policy. Of those cases, only one (in Georgia) rejected a contingency arrangement as contrary to

public policy.[3] There is plainly no conflict on the constitutional issue presented here.

Thus there is no apparent basis for a grant of certiorari. There is not even an arguable conflict in the lower court decisions, and the lack of controversy indicates that there is not an issue of exceptional importance. Moreover, as explained in the next section, the decision below is entirely consistent with this Court's prior decisions.

II. THE COMPENSATION OF TAX AUDITORS HERE DID NOT VIOLATE THE REQUIREMENTS OF DUE PROCESS.

The lack of controversy over whether due process proscribes compensating tax auditors on a percentage-fee basis is perhaps explained by the fact that the question is not a difficult one. This Court spoke to it indirectly in *Tumey v. Ohio*, 273 U.S. 437, 510 (1927). In *Tumey*, the Court had before it statutes that allowed a mayor acting as a judge to be compensated out of the fines he imposed. The statutes also provided for compensating of deputy marshals, detectives, and others by awarding a percentage of fines collected. *Id.* at 439. Although the Court held that paying the mayor, acting as judge, based on the fines

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[3] *Sears, Roebuck & Co. v. Parsons*, 260 Ga. 824, 835, 401 S.E.2d 4, 5 (1991). *But see General Electric Co. v. City of Bridgeport*, CV93 30 45 71 S (Conn. Super. Ct. Dec. 16, 1993); *Dillon Stores, Inc. v. Lovelady*, 253 Kan. 274, 280, 855 P.2d 487, 491 (1993); *General Motors Corp. v. State Tax Comm'n*, 200 Mich. App. 117, 121, 504 N.W.2d 10, 12 (1993), *appeal dismissed*, 509 N.W.2d 157 (Mich. 1993).

he imposed was a violation of due process, it also explicitly recognized in dicta that contingency arrangements in other contexts raise no due process concerns.

The *Tumey* Court made clear that the Constitution does not generally prohibit States from paying for the assistance of private citizens or from paying them on a percentage-fee basis:

> [T]he Legislature of a state may and often ought to stimulate prosecutions for crime by offering to those who shall initiate and carry on such prosecutions rewards for thus acting in the interest of the state and the people. The Legislature may offer rewards or a percentage of the recovery to informers. . . . It may authorize the employment of detectives.

273 U.S. at 445.

The compensation system here is, if anything, less problematic than the rewards and contingency arrangements approved in *Tumey*. As described in the Statement of the Case above, the auditors in Cabarrus County merely make a report to the assessor. This report is based on the taxpayer's own records. The assessor, in turn, considers not only the report, but also any information made available by the taxpayer in meetings between the assessor and the taxpayer. *See* N.C. Gen. Stat. § 105-312(d). The assessor – not the auditor – determines whether to make a discovery assessment and the amount of the discovery. *See id.* § 105-312(b).

The assessor's decision is subject to several levels of review. First, the taxpayer may appeal a discovery assessment to the county Board of Equalization and Review. *See*

N.C. Gen. Stat. § 105-322. If the taxpayer is dissatisfied with that Board's decision, it may appeal to the state Property Tax Commission for a *de novo* evidentiary hearing and decision. *See id.* § 105-288. Next, the taxpayer may appeal of right to the North Carolina Court of Appeals. *See id.* § 105-345. Finally, the taxpayer may seek review by the Supreme Court of North Carolina. *See id.* §§ 7A-30, 7A-31. Thus there are ample procedural protections built into the assessment process. The limited role played by the auditor and the multiple safeguards in connection with any assessment put to rest any due process concerns. *See Mathews v. Eldridge*, 424 U.S. 319 (1976).

At bottom, petitioner's due process argument rests on the proposition that contingent fees involve intolerable risks – a proposition with no support either in hard facts or in intuition. Contingency arrangements are commonplace throughout our society. They are well accepted in certain kinds of attorney-client relationships, in business, and in the reward situation described in *Tumey*. The widespread use of contingency arrangements is explained by their considerable benefits, of which this case provides a dramatic example. Without the compensation at issue here, a rural county would not have uncovered a massive tax underlisting by a large corporation.

Petitioner attempts to argue that a tax auditor is equivalent to an assessor, and the assessor is a judicial or prosecutorial official subject to strict due process requirements. Pet. at 15-16. This chain of reasoning breaks at the first link. As explained above, the auditor's role is clearly distinct from the assessor's. The assessor issues the discovery and has no financial interest in the outcome of any

audit. To equate the auditor with the assessor is like equating a detective with a judge or prosecutor.

Moreover, there is ample reason to doubt that even the assessor (as distinguished from the auditor) is a judicial or prosecutorial official. For example, this Court, in its most recent pronouncement on the subject, expressly stated that "[t]he governmental function of fixing the value for tax purposes has rarely, if ever, been a judicial function." *Arkansas Corp. Comm'n v. Thompson*, 313 U.S. 132, 142-43 (1941).[4] There is little force, then, to the argument that the tax auditor in this case should be subject to the same standard as the judicial officer in *Tumey*.

With respect to prosecutors, petitioners failed to raise below any argument regarding prosecutorial due process. *See, e.g., Illinois v. Gates*, 462 U.S. 213, 217 (1983) (declining to decide issue not previously presented in state court); *Delta Air Lines, Inc. v. August*, 450 U.S. 346, 362

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[4] Petitioner relies on isolated language from a case from more than half a century prior to *Arkansas Corp. Comm'n – Hagar v. Reclamation District No. 108*, 111 U.S. 701 (1884). In *Hagar*, the Court in passing referred to the duties of a tax assessor as judicial. *Id.* at 710. Nothing turned on this characterization, however.

In fact, the *Hagar* Court made clear that the due process requirements of notice and an opportunity to be heard did not apply to the decision of the assessor, but rather to administrative or judicial review of that decision. *Id.* at 710-11. That is, *Hagar* did not treat the assessor's decision as equivalent to that of a judge. In view of this treatment and in view of the subsequent discussion of the role of the assessor in *Arkansas Corp. Comm'n*, *Hagar*'s reference to the assessor's judicial activities sheds little light on the due process limits on compensation of assessors – much less on compensation of auditors.

(1981) (same). This Court in *Marshall v. Jerrico, Inc.*, 446 U.S. 238 (1980) found that the requirements for satisfying due process were less rigorous than for judges, but recognized the possibility that compensation of prosecutorial officials could in some future case raise constitutional problems. Whatever the due process limits on prosecutors might be, they would give little guidance here, because of the obvious distinctions between tax assessors and prosecutors. Moreover, the conduct of an assessor (as opposed to tax auditor) is not even at issue here. Petitioner's failure to raise this issue previously is itself a strong indicator of its lack of substance.

In sum, this Court's prior decisions either support the decision below (*Tumey, Arkansas Corp. Comm'n*) or have no bearing on it (*Marshall*). The soundness of the decision below argues against review here.

III. THE LACK OF A WELL-DEVELOPED RECORD AND LACK OF FINALITY MAKE REVIEW HERE PARTICULARLY INAPPROPRIATE.

In addition to the unimportance of the issue and the lack of merit to petitioner's argument, other considerations also argue against a grant of certiorari here. There was hardly any legal discussion in the decisions below. This lack of reasoning is not remedied by case law elsewhere; rather, there is almost no jurisprudence on the issue presented. The undeveloped state of the law not only suggests the lack of real significance to the issue, but also suggests that consideration of the issue would be at best premature.

Just as important, the issue presented here was decided below with hardly any factual development. There was no evidence presented in court or in administrative hearings as to the activities of tax auditors in Cabarrus County. Instead, petitioner relied on its counsel's representations as to those activities. These representations were disputed in certain respects (though similarly without record evidence) by counsel for respondent. Disputed issues included whether certain taxpayers were unfairly singled out for audits and what role the auditor played in the discovery process. The lack of a clear factual record and unresolved factual issues make this case a poor vehicle for clarifying any arguable uncertainty in the law.

Finally, the ongoing nature of the proceedings here argues against review. The decision below should not be deemed to satisfy the finality requirement of 28 U.S.C. § 1257, since the case was remanded for further state proceedings. To be sure, petitioner attempts to rely on the exception set forth in *Cox Broadcasting Corp. v. Cohn*, 420 U.S. 469, 480, 506 (1975) (majority and Rehnquist, J., dissenting) for federal questions "bound to survive . . . regardless of the outcome of future state-court proceedings." The question here, however, is not "bound to survive." In the remand proceedings, petitioner has attempted to present state-law arguments that, if accepted, would eliminate liability and moot the federal issue.

Of the four categories set out in *Cox*, the exception that comes closest to fitting this case is the fourth, for cases "with further proceedings pending in which the party seeking review here might prevail on the merits on

nonfederal grounds, thus rendering unnecessary review of the federal issue by this Court, and where reversal of the state court on the federal issue would be preclusive of any further litigation. . . . " 420 U.S. at 482-83. This exception applies, however, only "if a refusal immediately to review the state court decision might seriously erode federal policy. . . . " *Ibid.* Thus in *Flynt v. Ohio*, 451 U.S. 619, 622 (1981), this Court declined to apply the fourth *Cox* exception in the context of an Equal Protection Clause challenge alleging selective prosecution because "resolution of this question can await final judgment without any adverse effect upon important federal interests."

The same is true here: there is no important federal policy that would be undermined by putting off review until a final determination in the state proceedings. Even leaving aside the apparent lack of jurisdiction here, the possibility that petitioner will eventually prevail argues against a grant of certiorari. Particularly when added to the other strong reasons not to review this case (the lack of a conflict, lack of an important issue, and the soundness of the decision below), denial is appropriate since the case might become moot.

CONCLUSION

This case presents no conflict among state courts, no question of unusual importance, and no other reason to merit a place on this Court's docket. Even if there were some reason to examine the question presented, this case would present a number of problems, because of the

undeveloped state of the legal and factual record. Particularly given that state proceedings are still in progress, review here is unjustified. For all these reasons, respondent requests that the petition be denied.

This the 27 day of May, 1994.

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Supreme Court, U.S.
FILED
JUN 6 1994
OFFICE OF THE CLERK

No. 93-1710

IN THE

Supreme Court of the United States

OCTOBER TERM, 1993

PHILIP MORRIS INCORPORATED
(d/b/a PHILIP MORRIS U.S.A.),
Petitioner,

v.

CABARRUS COUNTY, NORTH CAROLINA,
Respondent.

On Petition for a Writ of Certiorari to the Supreme Court of North Carolina

PETITIONER'S REPLY TO BRIEF IN OPPOSITION

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RULE 29.1 STATEMENT

There has been no change in the information provided in the Rule 29.1 Statement in the Petition.

IN THE

Supreme Court of the United States

OCTOBER TERM, 1993

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PHILIP MORRIS INCORPORATED
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CABARRUS COUNTY, NORTH CAROLINA,

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On Petition for a Writ of Certiorari to the Supreme Court of North Carolina

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PETITIONER'S REPLY TO BRIEF IN OPPOSITION

I. Introduction

Respondent attempts to make five points in its brief in opposition: (1) the Due Process issue is not significant; (2) the record is not well developed for consideration of the issue; (3) the case law supports respondent's position in any event; (4) petitioner has raised a new issue at the certiorari stage; and (5) the case may become moot because petitioner may prevail in the remand proceedings.

For the reasons indicated below, none of these points justifies a denial of the petition.

II. Respondent's First Four Points Have No Merit

1. Contrary to respondent's view, the Due Process issue is quite significant. It potentially affects all business taxpayers in Cabarrus County and countless business taxpayers located in other counties in North Carolina, as well as in Kansas, Wyoming, Connecticut and possibly in other states as well. It raises fundamental questions regarding the propriety of the tax assessment process conducted by local governments in various parts of the United States.

2. The record is quite well developed for purposes of this Court's consideration of the issue. The following points are clear:

—with no funds for staff auditors, respondent retained TMA under a contingent fee agreement to assist the County Assessor by conducting personal property tax audits of business taxpayers (Resp. Br. Opp. 5; Pet. App. 22a-24a);

—the agreement with TMA provided for a fee equal to 35 percent of "taxes discovered," with partial payment to be made on issuance of the discovery notice (Pet. App. 23a);

—under the agreement, TMA would receive no fee whatever if it failed to "discover" new taxes; conversely, the more taxes it discovered, the greater the fee it stood to receive (Pet. App. 22a-24a);

—"as a direct result" of the agreement, TMA conducted a personal property tax audit of petitioner, the largest taxpayer in the County (Pet. App. 9a, 24a);

—TMA issued a report to respondent's Assessor proposing a "discovery" of $975 million of property (Pet. App.58a); and

—based on TMA's report, the Assessor issued a discovery, presumed to be correct, in the amount of $923 million (Resp. Br. Opp. 4; Pet. App. 33a).

Those facts are all that is necessary to establish a Due Process violation here.[1]

3. The relevant case law clearly supports petitioner, not respondent. Respondent's effort to squeeze something helpful out of *Tumey* v. *Ohio*, 273 U.S. 510 (1927), falls far short of the mark. Respondent apparently quotes *Tumey* as it does because it believes that the work of TMA is similar to that of a detective, i.e., a mere fact gatherer. That is not the role of the business personal property tax auditor.

The tax auditor's job is to determine whether the return filed by the taxpayer satisfies the requirements of the law for reporting and valuing property. If it does not, the auditor proposes an assessment. That is a quasi-judicial or prosecutorial function, not a mere fact-gathering function. As the North Carolina Property Tax Commission stated in condemning the practice of using contingent fee auditors such as TMA:

> [I]t is the opinion of the Commission that sound tax policy is not served where individuals or organizations have a financial interest in the assessment of property tax or the amount collected. The implementation of such an *enforcement program* can only lead to abuses in the *enforcement system* or at the

[1] Interestingly, while arguing that the record is not sufficiently developed for consideration of the Due Process issue, respondent unabashedly laces its statement of the case with factual assertions that contain no citation to the record or to any other source. (Resp. Br. Opp. 2-5.)

> very least, the appearance to the public of such abuses.

Pet. App. 27a (emphasis added).

Whatever this Court may have intended by its references to the use of detectives in *Tumey*, it cannot be relevant here.

4. Petitioner has not raised any new issues at the certiorari stage. The constitutional issue raised throughout the proceedings is whether petitioner has been denied Due Process by virtue of respondent's use of TMA to conduct a tax audit of its personal property on a pure contingent fee basis. While emphasizing the application of *Tumey*, petitioner has pointed out the confusion created by this Court's prior decisions regarding the status of a tax assessor as a judicial or quasi-judicial official. In its petition, petitioner has argued that if respondent's Assessor is not acting in a judicial capacity subjecting him (through TMA as his agent) to the *Tumey/Ward* line of cases, he must be acting in a prosecutorial capacity, thereby implicating the Due Process concerns expressed in *Marshall* v. *Jerrico, Inc.*, 446 U.S. 238 (1980).

Petitioner's argument does not constitute the raising of a new issue at the certiorari stage; it is merely " 'but another ground or reason for alleging the invalidity of the [lower court's] judgment.' " *Illinois* v. *Gates*, 462 U.S. 213, 219-20 (1983) (quoting *Dewey* v. *Des Moines*, 173 U.S. 193, 197-98 (1899)).

III. The Judgment of the Court Below Satisfies the Finality Requirement

Respondent also contends that the judgment below is not final. Respondent reasons that if, on remand,

petitioner's tax liability were computed in the manner for which petitioner contends, petitioner's liability could be completely eliminated.[2]

Unfortunately, respondent's contention is not valid. Not only is petitioner not entitled to a true *de novo* review of the assessment before the Property Tax Commission, but under state law petitioner is effectively entitled to *no review* of any "insubstantial" adjustments proposed by TMA. As petitioner explained in its petition, the findings of the Assessor are not reviewable unless they are both (1) arbitrary or illegal, and (2) create a "substantial" misvaluation of the taxpayer's property. (Pet. at 17-19. *See also In re Highlands Development Corporation*, 80 N.C. App. 544, 546, 342 S.E. 2d 588, 589 (1986).) It is therefore a virtual certainty that, even if all of petitioner's state law arguments which the Commission could properly entertain on remand were accepted, the federal Due Process issue would not be mooted.

If, however, the possibility of mootness is seen to exist, respondent itself nevertheless acknowledges that the instant case could fall within the fourth category of cases discussed in *Cox Broadcasting Corp.* v. *Cohn*, 420 U.S. 469, 482-83 (1975) (cases with further proceedings pending in which the petitioner might prevail on nonfederal grounds, but where reversal by this Court on federal grounds would end the litigation and where refusal immediately to review the state court decision "might seriously erode federal policy"). In

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[2] The hearing on remand was begun on May 9, 1994. Briefs were submitted on May 31, 1994. The decision of the State Property Tax Commission is expected shortly.

respondent's view, however, "there is no important federal policy that would be undermined" by delaying review at this time. (Resp. Br. Opp. 14.)

Respondent again fails to grasp the significance of the *Tumey/Ward* line of cases. Over a period of 67 years, those cases have established a clear federal policy of ensuring unbiased and disinterested adjudications at the local level. *See also Marshall* v. *Jerrico, Inc.*, 446 U.S. at 242.

The Due Process interest in ensuring the fair and impartial enforcement of local tax assessment laws seems overwhelming. If the issue here presented is not resolved at this time, the offensive practice under challenge will be allowed to continue for an indefinite period in North Carolina and in those other states that still permit it. Yet, as the Supreme Court of Georgia declared in considering the practice:

> The people's entitlement to fair and impartial tax assessments lies at the heart of our system, and, indeed, was a basic principle upon which this country was founded.

Sears, Roebuck & Co. v. *Parsons*, 260 Ga. 824, 825, 401 S.E. 2d 4, 5 (1991).

The words of the Georgia Supreme Court are as much words of Due Process as they are words of public policy. They underscore the point that fundamental federal principles are at stake in the instant case. Allowing an indefinite continuation of the contingent fee audit practice will significantly undermine the federal policy established by numerous decisions of this Court dating back to 1927. Under this Court's "pragmatic approach" to finality as described in *Cox*

Broadcasting, 420 U.S. at 486, the judgment below is final and reviewable by this Court.

If this Court remains concerned about the possibility of the case becoming moot on remand, it may wish to await the Commission's decision before acting on the petition. Because there is no prospect that the lower courts will reconsider petitioner's Due Process claim, however, this Court should not in any event require a further, fruitless trip by petitioner through the North Carolina court system merely to preserve the Due Process issue for the filing of a second petition for certiorari.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,

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June 6, 1994